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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1993

IN RE WELLS FARGO SECURITIES LITIGATION

WELLS FARGO & CO., *et al.*,
Petitioners,

v.

HOWARD GREENWALD, *et al.*,
Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

APPENDIX TO PETITION FOR WRIT OF CERTIORARI

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In re WELLS FARGO SECURITIES LITIGATION.

Howard GREENWALD; Milton Friedman; Sheldon Shore; John Paul Decker; Fairmont Financial Corporation; Arthur-Magna Inc; Harold Bloch; Robert C. Schilling, on behalf of themselves and all others similarly situated, Plaintiffs-Appellants,

v.

WELLS FARGO & CO., a Delaware Corporation; Carl E. Reichardt; Paul Hazen; Robert L. Joss; Clyde Ostler; David M. Petrone; William F. Zuendt; Stephen A. Enna; Rodney L. Jacobs; Patrick W. Leahy; Guy Rounsaville, Jr., Defendants-Appellees.

No. 92-15344.

United States Court of Appeals,

Ninth Circuit.

Argued and Submitted May 10, 1993.

Decided Dec. 29, 1993.

William S. Lerach, Milberg, Weiss, Bershad, Hynes & Lerach, San Diego, CA, and Elizabeth Joan Cabraser, Lieff, Cabraser & Heimann, San Francisco, CA, for plaintiffs-appellants.

Melvin R. Goldman, Morrison & Foerster, San Francisco, CA, for the defendants-appellees.

Appeal from the United States District Court for the Northern District of California.

Before: REINHARDT, TROTT, and RYMER, Circuit Judges.

RYMER, Circuit Judge:

Purchasers of Wells Fargo & Co. common stock ("shareholders") appeal from the district court's order dismissing their securities fraud class action with prejudice pursuant to Federal Rule of Civil Procedure 12(b)(6).[1] In their Amended Complaint, the shareholders allege that Wells Fargo & Co. and certain of its senior officers and directors (collectively "Wells Fargo") violated § 10(b) of the Securities Exchange Act of 1934 ("'34 Act"), 15 U.S.C. § 78j(b); the SEC's Rule 10b-5, 17 C.F.R. § 240.10b-5; § 20 of the '34 Act, 15 U.S.C. § 78t; and California Civil Code §§ 1709-10 by fraudulently withholding material information and by issuing a series of false and misleading statements relating to the level of loan loss reserves maintained by Wells Fargo & Co.'s banking subsidiary, Wells Fargo Bank.[2] The shareholders claim that these omissions and misrepresentations served to inflate artificially the trading price of Wells Fargo & Co. stock, thus causing financial injury to those who purchased the overpriced shares. We have jurisdiction under 28 U.S.C. § 1291, and we reverse.

I

On June 25, 1991, Wells Fargo & Co. issued a statement that Wells Fargo Bank would recognize $180 million in actual loan losses for the second quarter ending June 30, 1991, and that the Bank expected to add approximately $350 million to its loan loss reserves for that same period. Wells Fargo's disclosure precipitated a sharp drop in the trading price of its stock — from a pre-announcement high of $97 per share to $74 per share. Shareholders who purchased Wells Fargo stock between March 5, 1991, when the company issued its

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1. Although the district court mentioned Fed. R. Civ. P. 9(b) in its opinion, both sides agree that it did not rely on Rule 9(b) in ordering dismissal.

2. In dismissing the shareholders' cause of action under § 10(b) and Rule 10b-5, the district court did not reach the merits of either the shareholders' § 20 claim or their California state law claims for fraud and negligent misrepresentation. Accordingly, the propriety of the district court's dismissal of the shareholders' claim for relief under § 10(b) and Rule 10b-5 is the only issue on appeal.

1990 Annual Report to Shareholders and filed its Form 10-K with the SEC, and June 25, 1991, the date that Wells Fargo disclosed that it would increase loan loss reserves for the second quarter, filed their amended class action complaint on August 26, 1991.

The theory of securities fraud advanced by the shareholders' Amended Complaint is that Wells Fargo maintained the inflated trading price of its common stock by failing to disclose the status of certain loans that it knew were in jeopardy. More specifically, the shareholders allege that senior directors and officers of Wells Fargo, motivated by the desire to "continue and prolong the image of Wells Fargo as a well-managed enterprise with sound lending procedures" and thus, maximize their individual compensation, the value of their personal Wells Fargo & Co. stock holdings, and their job security, became aware in March 1991 that the Bank's commercial, real estate, and highly leveraged loan portfolios had been mismanaged, were "not fundamentally sound and [were] prone to non-repayment in foreseeable and predictable economic downturns." Nonetheless, according to the shareholders, Wells Fargo was able to maintain the high value of its stock "through the issuance of materially false and misleading reports filed with the SEC, annual and quarterly reports to shareholders, releases to the public and financial statements," all intended to conceal "how poorly Wells Fargo had been managed by the Individual Defendants and how badly its financial and operating condition had deteriorated." Primary among Wells Fargo's alleged methods of deception was a deliberate understatement of loan loss reserves,[3] effected through Wells Fargo's failure timely to recognize known problem loans and failure to adjust loan loss reserves "at an appropriate level consistent with the [known] risk of loss actually faced."

In its Order Granting Defendants' Motion to Dismiss the shareholders' complaint for failure to state a claim, the district court held that "[n]othing in plaintiffs' voluminous complaint states facts which support a coherent theory of securities fraud." The court concluded

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3. The Amended Complaint states that banks charge each quarter's provision for loan losses against current net income, thu .educing earnings per share in an amount corresponding to the increase in the reserve.

that the shareholders' Amended Complaint alleged non-actionable "fraud by hindsight," and characterized the shareholders' suit, purportedly based on a three-month conspiracy among the defendants to conceal or misrepresent the Bank's financial health by understating loan loss provisions, as one more accurately describing mismanagement by Wells Fargo, or perhaps a violation of the applicable banking regulations. As the district court explained, "[t]he fact that defendants increased loan loss reserves in the second quarter, and at all times relevant accurately reported the amount of actual reserves set aside by the bank, does not by itself allege securities fraud, notwithstanding conclusory statements of fraud in the complaint." Stating that the shareholders' Amended Complaint, "a collaborative effort by a dozen law firms with significant experience in [the] field of securities litigation," "cannot be further improved," the district court granted Wells Fargo's motion to dismiss the federal securities law causes of action with prejudice. Finally, pursuant to 28 U.S.C. § 1367(c)(3), the court declined to exercise its supplemental jurisdiction to hear the shareholders' two remaining state law claims.

II

A dismissal for failure to state a claim pursuant to Federal Rule of Civil Procedure 12(b)(6) is a ruling on a question of law and as such is reviewed de novo. *Oscar v. University Students Co-op. Ass'n*, 965 F.2d 783, 785 (9th Cir.) (en banc), *cert. denied*, ___ U.S. ___, 113 S.Ct. 655, 121 L.Ed.2d 581 (1992). All allegations of material fact are taken as true and construed in the light most favorable to the plaintiff. *Love v. United States*, 915 F.2d 1242, 1245 (9th Cir. 1989).

III
A

The shareholders contend that the allegation that Wells Fargo intentionally or recklessly understated its loan loss reserves in an effort to inflate corporate earnings (and therefore earnings per share), and then disseminated financial statements reflecting this misallocation to the public and to the SEC, states a claim under § 10(b) and Rule 10b-5. Noting that a bank's loan loss reserve is set based on the risk

of loss posed by the aggregate of a bank's loan transactions, the shareholders argue that the deliberate failure to recognize problem loans, thus understating the reserve, constitutes an actionable omission or misrepresentation of existing fact which cannot be dismissed as a mere matter of internal mismanagement, unsound business practice, or poor accounting judgment.

The shareholders are correct. To state a claim under § 10(b) and Rule 10b-5, the shareholders must allege that Wells Fargo knowingly or recklessly published an "untrue statement of fact" or omitted to state a material fact "necessary to make the statements made, in light of all the circumstances in which they were made, not misleading." *In re Apple Computer Sec. Litig.*, 886 F.2d 1109, 1113 (9th Cir. 1989), *cert. denied*, 496 U.S. 943, 110 S.Ct. 3229, 110 L.Ed.2d 676 (1990). Wells Fargo's financial statements contain no "untrue statements of fact" — the shareholders do not dispute that Wells Fargo accurately disclosed the amount allocated by the Bank to its loan loss reserves. Thus, the shareholders must identify some omission of material fact necessary to make Wells Fargo's literally accurate reporting of the size of its reserve not misleading. In substance, the shareholders allege that Wells Fargo's statement of its loan loss reserves failed to disclose — *i.e.*, failed to reflect — certain loans that Wells Fargo knew were "in jeopardy." The shareholders list a representative selection of those bad loans which, in their view, Wells Fargo should have recognized by adjusting its reserves accordingly. Alleged problem loans, of which Wells Fargo was "on notice" prior to the start of the Class Period and failed properly to disclose, include loans extended to Revco D.S., Insilco Corp., Charter Medical Corp., R.H. Macy & Co., Campeau Corp., Jim Walters Corp., Gaylord Container Corp., West Point Pepperell, Inc., and NWA, Inc. The shareholders allege that Wells Fargo's non-performing assets and its reserves for possible loan losses were understated by at least $400 million and $350 million respectively, due to defaults on and the doubtful collectability of a number of its loans.

Accurate information regarding a bank's specific, substantial loans, with respect to which the alleged understating of value totals nearly $400 million in this case, cannot be deemed non-material as a

matter of law. In *Shapiro v. UJB Fin. Corp.*, 964 F.2d 272, 276-77 & n. 6 (3d Cir.), *cert. denied*, ___U.S. ___, 113 S.Ct. 365, 121 L.Ed.2d 278 (1992), plaintiffs alleged that UJB Corp. fraudulently inflated its "earnings, assets, and net worth" by understating "its non-performing loans" and by failing "to provide adequate loan loss reserves for problem loans promptly and properly." The plaintiffs further alleged that UJB issued a series of statements which "misrepresented the true status of the company's loan loss reserves, financial health, lending practices, and internal controls." *Id.* at 280.[4] The court stated:

> There is nothing unique about representations and omissions regarding loan loss reserves that removes them from the purview of the antifraud provisions of the federal securities laws. In our view a reasonable investor would be influenced significantly by knowledge that a bank has knowingly or recklessly hidden its true financial status by deliberately misstating its level of non-performing loans, failing to provide adequate reserves, and indulging its problem loan customers.

Id. at 281.

Wells Fargo initially asserts that "an increase in the loan loss reserve, without more, does not warrant an inference of fraud," and "that an increase in the loan loss reserve from one quarter to the next does not alone imply that earlier estimates of the reserve were fraudulently understated." Yet, the shareholders' allegations do aver "something more": the deliberate failure to disclose the status of certain specific loans extended to identified borrowers. Wells Fargo responds that the Amended Complaint is deficient because it does not state how much the nine named corporations borrowed; when the loans were made; whether these loans were in default and, if so, when the default occurred; or whether reserves should have been established (but were not), and, if so, when and on what basis. However, this level of specificity is not required at the pleading stage. *See Moore v. Kayport Package Express, Inc.*, 885 F.2d 531, 540 (9th Cir. 1989) ("A pleading is sufficient under rule 9(b) if it identifies the circumstances

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4. *See* Part III-B *infra*.

constituting fraud so that a defendant can prepare an adequate answer from the allegations.").

Wells Fargo's principal contention is that the shareholders' allegations amount to non-actionable mismanagement, not actionable securities fraud. It relies on *Santa Fe Indus. v. Green*, 430 U.S. 462, 97 S.Ct. 1292, 51 L.Ed.2d 480 (1977), in which the Court held that "Congress by § 10(b) did not seek to regulate transactions which constitute no more than internal corporate mismanagement." *Id.* at 479, 97 S.Ct. at 1304. Characterizing the shareholders' Amended Complaint as one which challenges the timing of Wells Fargo's disclosure or some other "material deficiency in the administration of the loan loss reserve," Wells Fargo emphasizes that the calculation of reserves is an uncertain, "dynamic" process, and necessarily is based in large part on the judgment and discretion of corporate management. While the setting of loan loss reserves is, by all accounts, an "art and not a science," we do not believe that the broad corporate management exclusion from § 10(b) and Rule 10b-5, set forth in *Santa Fe*, is implicated when plaintiffs allege specific misrepresentations or material nondisclosures in violation of the federal securities laws. *See Virginia Bankshares, Inc. v. Sandberg*, ___ U.S. ___, ___ n. 6, 111 S.Ct. 2749, 2758 n. 6, 115 L.Ed.2d 929 (1991) ("Although a corporate transaction's 'fairness' is not, as such, a federal concern," a corporation's published claim of fairness 'presupposes a factual integrity that federal law is expressly concerned to preserve"); *Hayes v. Gross*, 982 F.2d 104, 106 (3d Cir. 1992) ("[A]n allegation of mismanagement on the part of a defendant will not alone support a claim under § 10(b) or Rule 10b-5; nor will an allegation that a defendant failed to disclose the existence of mismanagement. ... [H]owever, ... a complaint does allege an actionable misrepresentation if it alleges that a defendant was aware that mismanagement had occurred and made a material public statement about the state of corporate affairs inconsistent with the existence of the mismanagement."). That Wells Fargo's loan reserves were inadequate throughout the relevant period is not in serious dispute; "rather, the question [is] whether the inadequacy was in some sense culpable because the contingencies which proved them inadequate were foreseen or foreseeable." *Blackie v. Barrack*, 524 F.2d 891, 904 (9th Cir. 1975), *cert. denied*, 429 U.S. 816,

97 S.Ct. 57, 50 L.Ed.2d 75 (1976); *see also Urbach v. Sayles*, 779 F. Supp. 351, 354-55 (D.N.J. 1991) ("Although a manager may never 'know' with absolute certainty that a reserve against anticipated losses is inadequate, there will be circumstances where she 'knows,' based on any plausible and acceptable means of calculation, projection, or forecast, that reserves must be increased and yet represents that they need not be."). The shareholders allege that Wells Fargo knew of certain "contingencies" which rendered its loan reserves "inadequate," and failed to disclose this information to purchasers of its stock.

Therefore, taking the allegations of the Amended Complaint to be true, as the court must on a Rule 12(b)(6) motion, this is neither a case second-guessing decisions by management nor one alleging "fraud by hindsight"; rather, the shareholders have specifically identified facts omitted by Wells Fargo, which if subsequently determined to be material, and issued by Wells Fargo with the requisite scienter, will establish a violation of § 10(b) and Rule 10b-5. The cases upon which Wells Fargo places most weight do not dictate a different result, because unlike the present situation, the plaintiff in each of the cited decisions failed to point to alleged facts suggesting that the defendant's failure to disclose its "financial deterioration[ ]" was "attributable to fraud." *DiLeo v. Ernst & Young*, 901 F.2d 624, 626-27 (7th Cir.) (complaint did not "give examples of problem loans that [the accounting firm] should have caught, or explain how it did or should have recognized that the provisions for reserves established by [the bank's] loan officers were inaccurate"), *cert. denied*, 498 U.S. 941, 111 S.Ct. 347, 112 L.Ed.2d 312 (1990); *see also Christidis v. First Pennsylvania Mortgage Trust*, 717 F.2d 96, 100 (3d Cir. 1983) (complaint's "defect [was] the complete absence of any disclosure of the manner in which, in establishing reserves for bad debts in the financial statements relied upon, the defendants knowingly departed from reasonable accounting practices"); *Denny v. Barber*, 576 F.2d 465, 469 (2d Cir. 1978) (complaint failed to specify "what loans, at what times, and in what amounts were 'risky,'" or which items in defendant's annual report were knowingly false). Here, the shareholders' allegations successfully "distinguish their situation from that of many other[ ] [investors] who are adversely affected by business reverses." *DiLeo*, 901 F.2d at 627.

B

The shareholders contend that, in addition to sending a misleading message to the market in its financial reports, Wells Fargo "made affirmative representations inconsistent with the state of corporate affairs they knew to exist." *Hayes*, 982 F.2d at 106. The shareholders allege that Wells Fargo falsely portrayed itself as a successful company with favorable future prospects for growth and profit, concealed that many of Wells Fargo's highly leveraged transaction ("HLT") and real estate loans were high-risk in character and near default, and failed to disclose Wells Fargo's non-compliance with banking and accounting regulations governing the treatment of such problem loans. The shareholders allege that Wells Fargo knew or should have known that its various statements, while often literally accurate, "contributed to an overall misleading impression of the financial condition and business prospects of Wells Fargo."[5]

For example, the shareholders allege that Wells Fargo's 1990 Annual Report falsely "reassured the investing public":

> The year 1990 was marked by the threat of war in the Persian Gulf, a faltering economy and a continuous stream of bad news affecting the nation's financial services industry.
>
> In these unsettled times, investor concerns about what lay ahead for Wells Fargo and the California economy largely overshadowed the Company's steady financial performance.
>
> Net income for the year rose 18%, to $711.5 million. Earnings per common share were $13.39, an increase of 22% in comparison with last year's $11.02 per share.
>
> * * * * * *

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5. Wells Fargo argues that these quotations are incomplete and are "wrenched out of context or edited in ways that change meaning." We disagree. Several of the shareholders' claimed misstatements identified by Wells Fargo are taken from the Appellants' Opening Brief, not the Amended Complaint. Other examples of "selective quotation" offered by Wells Fargo, while certainly presenting information in a manner favorable to the shareholders, are neither misleading nor unfair.

Defensive actions — redoubling surveillance of our real estate and corporate loan portfolios, working out arrangements with delinquent borrowers, trimming back corporate and real estate banking activities, increasing loan loss reserves, and strengthening the Company's capital base — occupied an increasingly important place in our day-to-day agendas.

* * * * * *

With the bulk of its loans and practically all of its deposits concentrated in California, Wells Fargo Bank has been a major contributor to — and beneficiary of — the state's economic growth.

* * * * * *

In short, we remain optimistic about California's prospects — and we still believe that our sharply focused regional marketing strategy is right for Wells Fargo. Over the years Wells Fargo has adopted a number of lending practices, pricing policies and credit standards designed to compensate for, and partly offset, the risks inherent in banking real estate and corporate credits. These practices have worked well for us in the past, and we believe they are especially appropriate to today's relatively high-risk banking environment.

* * * * * *

But in the final analysis, whatever success we've had in corporate and real estate lending is due to two things: good customers and a well-seasoned team of senior lending officers.

* * * * * *

Among other things, experience has taught us to anticipate and react quickly to potential problems — and to recognize small problems before they become big ones. It has also taught us to place as much faith in our analysis of our borrowers' integrity and their ability to pay as in the value of their collateral.

With respect to HLT loans, Wells Fargo's 1990 Annual Report stated:

> During the 1980s, Wells Fargo's Corporate Banking Group assisted in financing the restructuring, acquisition or buyout of slightly more than one hundred American corporations. Typically, Wells Fargo acted as lead banker and senior lender in these highly leveraged transactions (HLTs), providing secured term loans with average maturities of five to seven years. Normally, repayment schedules were based on reasonable projections of cash flow from operations, rather than the sale of corporate assets.
>
> * * * * * *
>
> The risks related to our HLT portfolio differ in two significant respects from those involved in real estate lending. First, the HLT portfolio is widely diversified, both geographically and by industry. Second, our experience in this type of lending has not been tested by recession. These differences make it more difficult to anticipate how the HLTs as a group will perform over the next 12 months. All we can say with certainty is that we will be exercising even more than our customary diligence in managing our HLTs as well as all other segments of our loan portfolio in coming months.
>
> * * * * * *
>
> The Company believes at the present time that these loans are substantially secured by the assets of the borrowers. In addition, at December 31, 1990 and 1989, senior HLT loans past due 90 days and still accruing were $8 million and $209 million, respectively. There were no HLT loans on restructured status and there was no ORE resulting from HLT loans at December 31, 1990 and 1989. Senior HLT loans of $36 million and $30 million were charged off in 1990 and 1989, respectively. During an economic downturn or a sustained period of rising interest rates, HLT borrowers may experience a decrease in their financial performance greater than that of non-HLT borrowers.

The shareholders allege that with respect to non-HLT loans, Wells Fargo "supplied numerous charts and tables, none of which warned the investing public of the full extent of the risks inherent there." The shareholders allege that Wells Fargo stated:

> The Company's determination of the level of the allowance, and correspondingly, the provision for loan losses

> rests upon various judgments and assumptions including, but not limited to, general economic conditions, loan portfolio composition and prior loan loss experience. The Company considers the allowance for loan losses of $885.4 million adequate to cover losses inherent in loans; commercial, real estate and other loan commitments; and standby letters of credit as of December 31, 1990.

Further, the shareholders allege that in subsequent SEC filings and financial statements, Wells Fargo falsely represented that its reported data "included all adjustments and provisions necessary for fair presentation of its results in conformity with Generally Accepted Accounting Principles ('GAAP')," Regulatory Accounting Principles ("RAP"), and various banking regulations. Finally, the shareholders allege that in a June 1991 article in *Barrons'* financial weekly, Wells Fargo dismissed the claim that the Bank would face an increase in non-performing real estate loans for the second quarter of 1991, and in response to media inquiries following a drop in the trading price of Wells Fargo stock on June 24, 1991, Wells Fargo stated that "it knew of no reason to explain" the drop in its stock price.

Where a defendant affirmatively characterizes management practices as "adequate" or loans as "substantially secured," "a defendant declares the subject of its representation to be material to the reasonable shareholder, and thus is bound to speak truthfully." *Shapiro*, 964 F.2d at 282. Statements of reasons, opinions, or beliefs are "factual" for purposes of the securities laws, and thus are actionable under § 10(b), if "one of three implied factual assertions is inaccurate: (1) that the statement is genuinely believed, (2) that there is a reasonable basis for that belief, and (3) that the speaker is not aware of any undisclosed facts tending to seriously undermine the accuracy of the statement." *Hanon v. Dataproducts Corp.*, 976 F.2d 497, 501 (9th Cir. 1992) (quotation marks and citation omitted); *see also Mayer v. Mylod*, 988 F.2d 635, 639 (6th Cir. 1993).

At least two of the Wells Fargo statements upon which the shareholders rely may be opinions of the sort classified as "factual" for purposes of § 10(b): "[t]he Company believes at the present time that these [HLT] loans are substantially secured by the assets of the borrowers" and "[t]he Company considers the allowance for loan losses

of $885.4 million adequate." Because we believe at least these two statements cannot be dismissed as non-actionable as a matter of law, we do not examine in detail each of the other allegations that the shareholders make. We do note, however, that the vast majority of the "deceptive" statements catalogued in the shareholders' Amended Complaint are not alleged to be factually inaccurate and pertain to Wells Fargo's past performance. These are clearly not materially misleading. *See In re Convergent Technologies Sec. Litig.*, 948 F.2d 507, 513 (9th Cir. 1991) ("The challenged statements do not imply any comparison between the rate of past and future growth. They simply report past performance and assert specific limited predictions for the future."). Whether other statements by Wells Fargo are actionable, such as allegations that Wells Fargo failed to comply with various accounting rules and banking regulations governing classification of loans and public disclosure, depends on whether the shareholders can make out the existence of an underlying material misstatement or omission of which Wells Fargo had knowledge. We leave further analysis to the district court.

The shareholders have specifically identified Wells Fargo's allegedly misleading statements and, as discussed in Part III-A, allege that these statements were not believed by Wells Fargo when published, lacked any reasonable basis, and were made despite known, undisclosed facts tending seriously to undermine their accuracy. Accordingly, the shareholders have stated a claim under § 10(b) and Rule 10b-5. While it may well turn out, as Wells Fargo maintains, that the contested statements are neither material nor misleading when considered in context, that is a determination better made on the kind of record which a motion for summary judgment affords.[6]

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6. The shareholders also argue that their allegation that Wells Fargo failed to comply with the mandate of SEC Regulation S-K, Item 303 states an actionable securities fraud claim under §10(b). *See* 17 C.F.R. § 229.303(a)(3)(ii). Acknowledging that Regulation S-K does not provide an independent cause of action, the shareholders contend that an SEC filing which does not comply with Item 303 creates a "false and misleading impression," and thus is highly relevant for purposes of determining whether a violation of § 10(b) and Rule 10b-5 has occurred. We do not reach this point in light of our disposition of their claims under Rule 10b-5.

IV

Wells Fargo argues that the shareholders have failed to allege facts which provide a basis for the inference of scienter.[7] Contrary to Wells Fargo's assertion, the shareholders allege facts to show that Wells Fargo knew or recklessly ignored that its challenged statements were materially misleading, and that the Wells Fargo defendants "stood to receive more compensation because of the alleged non-disclosure of material information." While "allegation[s] of unusual insider trading by defendants immediately preceding the disclosure of negative news" may be, as Wells Fargo contends, a characteristic of a "typical securities fraud class action," they are not required. The allegations of motive and opportunity in the complaint are sufficient to establish a basis for inferring Wells Fargo's fraudulent intent. *Cf. Blake v. Dierdorff*, 856 F.2d 1365, 1369-70 (9th Cir. 1988) (allegations that corporate management distributed false and misleading information to protect their executive positions and substantial compensation, and to increase bonus compensation pled specific intent to commit mail fraud with the requisite particularity). The cases relied upon by Wells Fargo do not support its argument, as they involve appeals from either summary judgment or dismissals of complaints which were substantially more general and conclusory than the shareholders' in the present case. *See e.g. Apple Computer*, 886 F.2d at 1117 (no genuine issue of material fact as to scienter where plaintiffs produced no evidence controverting defendants' affidavits stating that contested statements were made in good faith); *California Architectural Bldg. Prods., Inc. v. Franciscan Ceramics, Inc.*, 818 F.2d 1466, 1469-72 (9th Cir. 1987) (summary judgment record contains no evidence that defendants had the requisite intent to defraud, nor did plaintiffs' claim make economic sense), *cert. denied*, 484 U.S. 1006, 108 S.Ct. 698, 699, 98 L.Ed.2d 650 (1988); *Vaughn v. Teledyne, Inc.*, 628 F.2d 1214, 1220 (9th Cir. 1980) (plaintiffs present no probative evidence relevant to the issue of intent to defraud); *see also Wexner v. First Manhattan Co.*, 902 F.2d 169, 172-73 (2d Cir. 1990) (affirming dismissal of complaint where plaintiffs failed to allege general details of securities

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7. Wells Fargo's claim that the shareholders failed sufficiently to plead scienter was not addressed directly by the district court.

fraud conspiracy, how defendants knew contested statements to be false, roles of individual defendants, or how defendants stood to gain as a result); *Connecticut Nat'l Bank v. Fluor Corp.*, 808 F.2d 957, 961-62 (2d Cir. 1987) (according to facts pled, no plausible economic incentive for defendants to deceive shareholders).

V

The shareholders read the district court's Order Granting Defendants' Motion to Dismiss as holding that the shareholders failed to meet the "in connection with" requirement of a § 10(b) claim — *i.e.*, that Wells Fargo's alleged fraud was employed "in connection with" the purchase or sale of securities. While the shareholders' interpretation is reasonable based on certain language in the district court's order (*e.g.*, the "fraud alleged must 'touch' upon securities transactions") and the court's citation to *SEC v. Clark*, 915 F.2d 439, 449 (9th Cir. 1990), we need not decide this issue as Wells Fargo effectively concedes that the "in connection with" requirement was met.

VI

We conclude that the shareholders have stated a claim under section 10(b) of the '34 Act and Rule 10b-5. Accordingly, we reverse the district court's order dismissing the shareholders' Amended Complaint.

REVERSED.

TROTT, Circuit Judge, dissenting.

I respectfully dissent, and I do so essentially because I believe our colleague on the district court had it right when he dismissed this complaint for failure to state a claim. I can do no better than repeat the essence of his analysis:

> In order to survive a motion to dismiss, plaintiffs who allege securities fraud must plead facts which, if true, con-

stitute fraud. Fed.R.Civ.Proc. 9(b). Plaintiffs are not required to assert facts pertaining to fraud that are "peculiarly within the opposing party's knowledge," but the requirements of Rule 9(b) are satisfied only if the allegations of fraud are accompanied by a statement of the facts upon which the fraud is founded. *Wool v. Tandem Computers, Inc.*, 818 F.2d 1433, 1439 (9th Cir. 1987) (citations omitted).

Furthermore, plaintiffs' facts, and the inferences which reasonably can be drawn from them, must support a claim of fraud in the purchase or sale of securities. The federal securities laws do not proscribe all fraud which occurs in the business world. The fraud alleged must "touch" upon securities transactions. *S.E.C. v. Clark*, 915 F.2d 439, 449 (9th Cir. 1990).

Nothing in plaintiffs' voluminous complaint states facts which support a coherent theory of securities fraud. Plaintiff's (sic) theory begins with heightened federal regulatory guidelines, issued in January, March and May of 1991, which suggested (but did not require) changes in the methods banks use to value nonaccrual loans and highly leveraged transactions. Plaintiffs then describe what they allege to be a three month long "scheme" by the defendants to misrepresent the Bank's financial health through understated loan loss provisions for the first quarter of 1991. Despite a complaint of 59 pages, containing 134 paragraphs of allegations, plaintiffs' counsel was unable to point to one paragraph or set of paragraphs which provide the facts necessary to infer fraud in the purchase of (sic) sale of securities.

Indeed, the facts in the complaint, which may suggest mismanagement on the part of the Bank, and might even suggest a violation of banking regulations, cannot be fairly read to raise an inference that the alleged misconduct by the defendants touched upon a securities transaction. The fact that defendants increased loan loss reserves in the second quarter, and at all times relevant accurately reported the amount of actual reserves set aside by the bank, does not by itself allege securities fraud, notwithstanding conclusory statements of fraud in the complaint.

Judge Friendly, in adjudicating a securities fraud claim from an earlier period of financial reversals in the banking industry, characterized a complaint similar to the one filed in this matter as "an example of alleging fraud by

> hindsight." *Denny v. Barber*, 576 F.2d 465, 470 (2d Cir. 1978). Judge Friendly recognized the difficulties encountered by a small shareholder in framing a securities fraud complaint against a large corporation, and the consequent need to relax pleading requirements, but dismissed the complaint in *Denny* because "there still must be more than vague allegations that, as shown by subsequent developments, the corporation's true financial picture was not so bright in some respects as its annual reports had painted and that the defendants knew, or were reckless in failing to know, this." *Id.*
>
> In the argot of today, a complaint should be dismissed if, read as a whole, it creates a strong impression that, on a report of bad news from the defendant, "plaintiffs' counsel simply stepped to the nearest computer console, conducted a global Nexis search, pressed the 'Print' button, and filed the product as their complaint." *Hershfang v. Citicorp*, 767 F.Supp. 1251 (S.D.N.Y. 1991). Here, plaintiffs cite annual reports, quarterly reports, banking regulations and newspaper articles. They list customers of the Bank who are known today to be burdened with debt. But nowhere does the complaint link the facts stated to a coherent theory of securities fraud.

Fraud on the market is a problematic theory. Unless carefully managed by us, it threatens to wrack our economy. Anytime a stock price drops significantly, will all prior rosy statements by management concerning the company's financial condition and future business prospects become the basis for actionable fraud?

I note with great interest that the supposedly defrauded stockholders in this case state in their complaint that "the trading price of Wells Fargo's common stock, upon disclosure [of the "fraud"] ... collapse[d] ... from over $97 per share to $74 per share." I note with equally great interest that the trading price of this stock on the day of oral argument, May 10, 1993, was $104.75. This is an interesting kind of fraud where the value of the disputed stock before the case goes to trial exceeds its value before the alleged wrongdoing that caused it to "collapse." I would suspect that on remand the district court will be confronted with an interesting motion for summary judgment.

When businesses complain about the costs heaped on them by a court system with no adequate controls, I believe they will be able to point to this litigation as an example.

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

In re: WELLS FARGO SECURITIES LITIGATION	**Master File No. NC-91-1944-VRW**
This Document Relates To: ALL ACTIONS.	**ORDER GRANTING DEFENDANTS' MOTION TO DISMISS**

[Filed December 21, 1991]

This matter came before the court on Thursday, December 5, 1991 on plaintiffs' motion for class certification and defendants' motion to dismiss the complaint for failure to state a claim upon which relief can be granted. Counsel for the parties had previously appeared before the court on Friday, November 1, 1991 on related motions. The court has considered the arguments of counsel, and the briefs, declarations and other documents filed in connection with this matter.

Plaintiffs' amended class action complaint purports to state federal claims under §§ 10(b) and 20 of the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder. Plaintiffs also assert claims under state law for fraud and negligent misrepresentation. The gravamen of plaintiffs' complaint is that Wells Fargo's banking subsidiary, Wells Fargo Bank ("the Bank"), defrauded investors by misstating the amount of loan loss reserves necessary to protect the Bank from default on high risk loans. Plaintiffs' allege that this activity began on March 5, 1991, when the Bank published in its annual report that it was, in accordance with recently-promulgated banking regulations, carefully monitoring its portfolio of high-risk loans. The alleged fraud continued through April 16, 1991, when the Bank reported first quarter loan loss reserves of $85 million. The fraud was

disclosed, according to plaintiffs, when the Bank announced on June 25, 1991 that it would increase loan loss reserves by $350 million in the second quarter.

Defendants' motion to dismiss is governed by Rules 9(b) and 12(b)(6) of the Federal Rules of Civil Procedure. In ruling on a motion to dismiss, district courts must accept all material allegations of fact alleged in the complaint as true, and resolve all doubts in favor of the plaintiff. *Blake v. Dierdorff*, 856 F.2d 1365, 1368 (9th Cir. 1988). A complaint may be dismissed as a matter of law for two reasons: (1) lack of a cognizable legal theory, or (2) insufficient facts under a cognizable theory. *Robertson v. Dean Witter Reynolds, Inc.*, 749 F.2d 530, 533-34 (9th Cir. 1984) (citing 2A J. Moore, Moore's Federal Practice, ¶ 12.08 at 2271 (2d ed. 1982)).

In order to survive a motion to dismiss, plaintiffs who allege securities fraud must plead facts which, if true, constitute fraud. Fed. R. Civ. Proc. 9(b). Plaintiffs are not required to assert facts pertaining to fraud that are "peculiarly within the opposing party's knowledge," but the requirements of Rule 9(b) are satisfied only if the allegations of fraud are accompanied by a statement of the facts upon which the fraud is founded. *Wool v. Tandem Computers, Inc.*, 818 F.2d 1433, 1439 (9th Cir. 1987) (citations omitted).

Furthermore, plaintiffs' facts, and the inferences which reasonably can be drawn from them, must support a claim of fraud in the purchase or sale of securities. The federal securities laws do not proscribe all fraud which occurs in the business world. The fraud alleged must "touch" upon securities transactions. *S.E.C. v. Clark*, 915 F.2d 439, 449 (9th Cir. 1990).

Nothing in plaintiffs' voluminous complaint states facts which support a coherent theory of securities fraud. Plaintiff's [sic] theory begins with heightened federal regulatory guidelines, issued in January, March and May of 1991, which suggested (but did not require) changes in the methods banks use to value nonaccrual loans and highly leveraged transactions. Plaintiffs then describe what they allege to be a three month long "scheme" by the defendants to misrep-

resent the Bank's financial health through understated loan loss provisions for the first quarter of 1991. Despite a complaint of 59 pages, containing 134 paragraphs of allegations, plaintiffs' counsel was unable to point to one paragraph or set of paragraphs which provide the facts necessary to infer fraud in the purchase of [sic] sale of securities.

Indeed, the facts in the complaint, which may suggest mismanagement on the part of the Bank, and might even suggest a violation of banking regulations, cannot be fairly read to raise an inference that the alleged misconduct by the defendants touched upon a securities transaction. The fact that defendants increased loan loss reserves in the second quarter, and at all times relevant accurately reported the amount of actual reserves set aside by the bank, does not by itself allege securities fraud, notwithstanding conclusory statements of fraud in the complaint.

Judge Friendly, in adjudicating a securities fraud claim from an earlier period of financial reversals in the banking industry, characterized a complaint similar to the one filed in this matter as "an example of alleging fraud by hindsight." *Denny v. Barber*, 576 F.2d 465, 470 (2d Cir. 1978). Judge Friendly recognized the difficulties encountered by a small shareholder in framing a securities fraud complaint against a large corporation, and the consequent need to relax pleading requirements, but dismissed the complaint in *Denny* because "there still must be more than vague allegations that, as shown by subsequent developments, the corporation's true financial picture was not so bright in some respects as its annual reports had painted and that the defendants knew, or were reckless in failing to know, this." *Id.*

In the argot of today, a complaint should be dismissed if, read as a whole, it creates a strong impression that, on a report of bad news from the defendant, "plaintiffs' counsel simply stepped to the nearest computer console, conducted a global Nexis search, pressed the 'Print' button, and filed the product as their complaint." *Hershfang v. Citicorp*, 767 F. Supp. 1251 (S.D.N.Y. 1991). Here, plaintiffs cite annual reports, quarterly reports, banking regulations and newspaper

articles. They list customers of the Bank who are known today to be burdened with debt. But nowhere does the complaint link the facts stated to a coherent theory of securities fraud.

Plaintiffs' counsel cites nearly two dozen federal district court cases, from districts other than this one, in which courts have sustained complaints against financial institutions which allegedly pled facts similar to the complaint at issue here. Plaintiffs' Memorandum in Opposition to Defendants' Motion to Dismiss at 14, n. 9. Defendants' counsel counters with even more reported cases wherein "allegations such as those of the amended complaint" were found not to state a claim. Defendant's Memorandum in Support of Motion to Dismiss at 10-11, n. 7. Again, Judge Friendly's admonition is instructive: "We see no profit in attempting to analyze these decisions, which may or may not be consistent and each of which necessarily rests on its particular facts." *Denny*, 576 F.2d at 470. Similarly, the complaint at bar must stand or fall on its own terms, and in accord with well-established pleading requirements.

There can be no dispute that this complaint fails to state a claim under the federal securities laws. The question is whether to afford plaintiffs' counsel leave to try again. A dismissal without leave to amend is proper where "allegation of other facts consistent with the challenged pleading could not possibly cure the deficiency" in the complaint. *Albrecht v. Lund*, 845 F.2d 193, 195 (9th Cir. 1988). Plaintiffs hastily filed suit following the Bank's announcement of the increase in loan loss reserves. In fact, the first complaint in this matter was filed on the very day in which Wells Fargo made its announcement. The amended complaint, a collaborative effort by a dozen law firms with significant experience in field of securities litigation, was filed two months later. This complaint cannot be further improved. Additional litigation of this matter would only place an undue burden on the defendants and the shareholders of Wells Fargo. Accordingly, defendants' motion to dismiss the federal causes of action in the complaint is **GRANTED WITH PREJUDICE**.

Although federal courts have jurisdiction to hear state law claims which are supplemental to federal claims, a court may decline to ex-

ercise its supplemental jurisdiction over a claim if the court has dismissed all claims over which it has original jurisdiction. 28 U.S.C. § 1367(c)(3). Defendants' motion to dismiss the state law claims is **GRANTED WITH PREJUDICE**.

IT IS SO ORDERED.

DATED: December 20, 1991

/s/ VAUGHN R. WALKER
United States District Judge

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: WELLS FARGO SECURITIES LITIGATION

HOWARD GREENWALD; MILTON FRIEDMAN; SHELDON SHORE; JOHN PAUL DECKER; FAIRMOUNT FINANCIAL CORPORATION; ARTHUR-MAGNA INC; HAROLD BLOCH; ROBERT C. SCHILLING, on behalf of themselves and all others similarly situated,

Plaintiffs-Appellants

v.

WELLS FARGO & CO., a Delaware Corporation; CARL E. REICHARDT; PAUL HAZEN; ROBERT L. JOSS; CLYDE W. OSTLER; DAVID M. PETRONE; WILLIAM F. ZUENDT; STEPHEN A. ENNA; RODNEY L. JACOBS; PATRICK W. LEAHY; GUY ROUNSAVILLE, JR.,

Defendants-Appellees

No. 92-15344

D.C. No. CV-91-01944-VRW

ORDER

[Filed March 8, 1994]

Before: REINHARDT, TROTT and RYMER, Circuit Judges

The panel has voted to deny the petition for rehearing and to reject the suggestion for rehearing en banc.

The full court has been advised of the suggestion for en banc rehearing, and no judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 35(b).

The petition for rehearing is DENIED and the suggestion for a rehearing en banc is REJECTED.

[Designation of counsel omitted]

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

HOWARD GREENWALD, MILTON FRIEDMAN, SHELDON SHORE, JOHN PAUL DECKER, FAIRMOUNT FINANCIAL CORPORATION, ARTHUR-MAGNA, INC., HAROLD BLOCH, and ROBERT C. SCHILLING, On Behalf of Themselves and All Others Similarly Situated,

Plaintiffs,

vs.

WELLS FARGO & CO., a Delaware Corporation, and CARL E. REICHARDT, PAUL HAZEN, ROBERT L. JOSS, CLYDE W. OSTLER, DAVID M. PETRONE, WILLIAM F. ZUENDT, STEPHEN A. ENNA, RODNEY L. JACOBS, PATRICK W. LEAHY, and GUY ROUNSAVILLE, JR., individuals,

Defendants.

No. C 91 1944 VRW

CLASS ACTION

NOTICE OF MOTION AND MOTION TO DISMISS THE AMENDED CLASS ACTION COMPLAINT

Date: November 1, 1991
Time: 10:30 A.M.
Courtroom of the Honorable Vaughn R. Walker, U.S.D.J.

[Filed September 30, 1991]

TO: ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

PLEASE TAKE NOTICE that on November 1, 1991, at 10:30 A.M., or as soon thereafter as counsel may be heard, in the Courtroom of the Honorable Vaughn R. Walker, United States District Judge, 450 Golden Gate Avenue, San Francisco, California,

Wells Fargo & Co. and the individual defendants, by counsel, will and hereby do move this court, pursuant to Federal Rules of Civil Procedure 12(b)(6) and 9(b), for an order dismissing the Amended Class Action Complaint.

This motion is based on this Notice of Motion and Motion, the Memorandum in Support of Motion by Defendants to Dismiss Plaintiffs' Amended Complaint, the Declaration of Michael L. Zigler in Support of Defendants' Motion to Dismiss, and the [Proposed] Order Granting Defendants' Motion to Dismiss filed concurrently, on the pleadings and files in this action, and on such argument as may be presented at the hearing.

Dated: September 30, 1991

MELVIN R. GOLDMAN
JACK W. LONDEN
MICHAEL L. ZIGLER
WILLIAM N. GERSON
MORRISON & FOERSTER

By /s/ Michael L. Zigler
Attorneys for Wells Fargo & Co.
and the Individual Defendants

[Proof of Personal Service, Proof of Service By Mail, and Service List omitted]

[Designation of counsel omitted]

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

HOWARD GREENWALD, MILTON FRIEDMAN, SHELDON SHORE, JOHN PAUL DECKER, FAIRMOUNT FINANCIAL CORPORATION, ARTHUR-MAGNA, INC., HAROLD BLOCH, and ROBERT C. SCHILLING, On Behalf of Themselves and All Others Similarly Situated,

Plaintiffs,

vs.

WELLS FARGO & CO., a Delaware Corporation, and CARL E. REICHARDT, PAUL HAZEN, ROBERT L. JOSS, CLYDE W. OSTLER, DAVID M. PETRONE, WILLIAM F. ZUENDT, STEPHEN A. ENNA, RODNEY L. JACOBS, PATRICK W. LEAHY, and GUY ROUNSAVILLE, JR., individuals,

Defendants.

Civil No. C-91-1944-VRW

CLASS ACTION

AMENDED CLASS ACTION COMPLAINT FOR DAMAGES FOR VIOLATIONS OF THE FEDERAL SECURITIES LAWS; FRAUD AND NEGLIGENT MISREPRESENTATION

Plaintiffs Request A Trial By Jury

[Filed August 26, 1991]

All allegations made in this Complaint are based on information and belief, except those allegations that pertain to the named plaintiffs and their counsel, which are based on personal knowledge. Plaintiffs' information and belief is based, *inter alia*, on the investigation made by and through their attorneys.

INTRODUCTION AND OVERVIEW OF ACTION

1. This class action is filed on behalf of all purchasers of Wells Fargo & Company ("Wells Fargo" or the "Company") common stock, to remedy violations by Defendants during the period from March 5, 1991 through June 25, 1991 (the "Class Period"), of the federal securities laws and California statutory and common law doctrines.

2. This class action lawsuit arises out of the gross mismanagement of Wells Fargo by its officers and directors, which was accompanied by a pattern of deception accomplished through false and misleading statements issued by Defendants concerning Wells Fargo, its business, financial condition, results from operations, quality of its management and future business prospects to the securities markets between March 5, 1991 and June 25, 1991, which had the purpose and effect of artificially inflating the trading price of Wells Fargo's common stock, throughout that period and which, upon disclosure, ultimately resulted in the collapse of Wells Fargo common stock from over $97 per share to $74 per share. The officer and director Defendants' gross mismanagement also resulted in establishment of huge amounts of additional loan loss reserves in excess of $350 million, more than four times the loan loss reserves for the prior quarter, and actual loan losses in the second quarter of 1991 of $180 million, more than two and one-half times the loan losses reported in the prior quarter.

3. During the Class Period, Defendants disseminated or caused Defendant Wells Fargo to disseminate a series of materially false and misleading statements, failed to disclose material facts and failed to correct prior statements concerning the business and finances of Wells Fargo. At the time Wells Fargo was announcing the payment of shareholders' dividends, as well as continued growth and profitability, Defendants knew, or should have known, and failed to disclose to Plaintiffs and other purchasers of Wells Fargo stock, that the Company was experiencing losses due to its previously undisclosed investments in high-risk loans, and that banking regulators had issued a number of regulations and policy statements that would materially

impact Wells Fargo's income for 1991. In particular, disclosure of the financial impact of the long-standing and reckless lending practices of the Company's senior management in the late 1980's in connection with extremely risky highly-leveraged transactions ("HLT Loans") and extremely speculative real estate ventures caused the virtual collapse of the market prices of the common stock of Wells Fargo.

4. In March 1991, Wells Fargo officers and directors named as Defendants herein became aware that Wells Fargo was suffering large losses in its loan portfolio due, *inter alia*, to inadequate and reckless lending procedures and loan loss recognition policies which resulted in huge increases in non-performing assets in the face of already inadequate loan loss reserves, many of which were incurred in connection with Wells Fargo's HLT loans. These Defendants realized that if the true nature and extent of the losses that Wells Fargo had already suffered, as well as the full nature and extent of the losses it would suffer in the coming months, were revealed, Wells Fargo's stock price would collapse overnight, their gross mismanagement of the Bank would be exposed, its capital position would be gravely impaired and they would face, *inter alia*, the prospect of the loss of their executive positions, possible punitive regulatory actions and other adverse consequences. In order to avoid these untoward consequences for as long as possible and to attempt to cover up their misconduct and Wells Fargo's precarious financial condition, these Defendants commenced a scheme and conspired to deceive Wells Fargo's current shareholders and the financial marketplace with respect to the true nature of the losses already suffered by Wells Fargo and to be suffered in the foreseeable future by engaging in a common course of conduct and conspiracy to issue false and misleading statements, including false financial statements, concerning Wells Fargo. In furtherance of this scheme, on March 5, 1991, the Defendants misrepresented and understated the true nature of Wells Fargo's non-performing assets and loan loss problems in the 1990 Annual Report. Thereafter, Defendants continued their scheme by consistently understating the true amount of Wells Fargo's nonperforming loans and required loan loss reserves by hundreds of millions of dollars, by falsely representing that Wells Fargo directors would "be exercising *even more than our*

customary diligence in managing [Wells Fargo's] HLT, as well as other segments of [Wells Fargo's] loan portfolio in coming months." These foregoing representations lead [sic] analysts to estimate earnings per share for Wells Fargo common stock for 1991 and 1992 at $10.50 per share in each year. In addition to making these false and misleading statements, to further foster the false image of profitability, controlled growth, high-quality assets, effective lending controls and standards and competent management the Defendants were projecting, Defendants issued or caused Wells Fargo to issue materially false and misleading financial figures for the first quarter of fiscal 1991 by which Wells Fargo reported earnings per share of $2.86, well in excess of analysts expectations, due in large part to the grossly inadequate loan loss reserve provisions.

5. Finally, when the aforementioned material adverse facts were belatedly disclosed to the public, Wells Fargo common stock lost approximately one-third of its value, causing Plaintiffs and the Class millions of dollars in investment losses. In particular, the Company's common stock fell precipitously in value when Wells Fargo revealed that it would increase its loan loss reserves by $350 million (more than four times the $85 million, the amount the Company had previously set aside in the first quarter of 1991), and that total non-accrual loans had dramatically increased, all of which had previously been concealed from and not disclosed to the investing public, including Plaintiffs and the Class as defined here.

JURISDICTION AND VENUE

6. The Court has jurisdiction of the first cause of action pursuant to §27 of the Securities Exchange Act of 1934 (the "Exchange Act") (15 U.S.C. §78aa).

7. This Court has jurisdiction over the second and third claims for relief, which are so related to the federal claims that the claims form part of the same case or controversy under Article III of the United States Constitution, under principles of supplemental jurisdiction (28 U.S.C. §1367).

8. As more fully described herein, in connection with the acts alleged in this complaint, Defendants, directly or indirectly, continuously used the means and instrumentalities of United Sates [sic] interstate commerce throughout the Class Period, including the United States mails and interstate telephone and wire communications and the facilities of the United States national securities markets.

9. Plaintiffs bring this suit as a class action pursuant to §§10(b) and 20 of the Exchange Act (15 U.S.C. §§78j(b)) and 78t and Rule 10b-5 promulgated thereunder (17 C.F.R. §240.10b-5).

10. Venue is proper in this District pursuant to §27 of the Exchange [sic] and 28 U.S.C. §1391(b). A substantial portion of the events and conduct giving rights [sic] to the violations of law complained of here, including the sales of securities in preparation and dissemination to the investing public of false and misleading information, incurred, and emanated from, this District. In addition, the principal place of business of Wells Fargo is within this District and most or all of the Individual Defendants performed their duties as officers and directors of these entities within this District. In connection with the acts, conduct and other wrongs complained of here, Defendants directly and indirectly, used the means and instrumentalities of interstate commerce, including the United States mails and interstate telephone communications.

THE PARTIES

11. Plaintiff Howard Greenwald purchased 100 shares of Wells Fargo common stock on May 25, 1991 at a price of $95.22 per share in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby. Plaintiff Greenwald still maintains his interest in Wells Fargo common stock, which as a result of the material adverse facts described here, has plummeted in value.

12. Plaintiff Milton Friedman purchased 300 shares of Wells Fargo common stock on June 14, 1991 at the price of $90.70 per share

in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby. Plaintiff Friedman still maintains his interest in Wells Fargo common stock, which as a result of the material adverse facts described here, has plummeted in value.

13. Plaintiff Sheldon Shore purchased 100 shares of Wells Fargo common stock on June 24, 1991 at a price of $81.50 per share in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby.

14. Plaintiff Fairmount Financial Corporation purchased shares of Wells Fargo common stock during the Class Period in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby.

15. Plaintiff John Decker purchased shares of Wells Fargo common stock during the Class Period in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby.

16. Plaintiff Arthur-Magna, Inc. purchased shares of Wells Fargo common stock during the Class Period in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby.

17. Plaintiff Harold Bloch purchased 1000 shares of Wells Fargo common stock on May 14, 1991 in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby.

18. Plaintiff Robert C. Schilling purchased shares of Wells Fargo common stock during the Class Period in reliance on the integrity of the market and at prices inflated by defendants' misconduct during the Class Period and has been damaged thereby.

19. Defendant Wells Fargo is a Delaware corporation, with its principal place of business in this District. Wells Fargo is a bank holding company with subsidiaries engaged in commercial banking, investment advisory services and agricultural consumer financing.

20. Wells Fargo's business has been owning and controlling banks and bank-related affiliates. Wells Fargo common stock is registered with the Securities & Exchange Commission ("SEC") pursuant to § 12(g) of Exchange Act and its common stock is listed and actively traded through NASDAQ and on the New York and Pacific stock exchanges in an open and efficient market. As of April 30, 1991, Wells Fargo had 51,660,987 shares of common stock outstanding held by more than 31,554 owners of record.

21. Defendant Carl E. Reichardt ("Reichardt") is chairman of the Board of Directors and Chief Executive Officer of Wells Fargo. For 1990, Defendant Reichardt received total cash and other compensation from Wells Fargo valued at more than $1,468,333 including substantial amounts in incentive-based compensation paid by Wells Fargo. For the years 1988, 1989 and 1990, Defendant Reichardt has received incentive based cash bonuses from Wells Fargo of at least $2,225,000. Defendant Reichardt was the beneficial owner of 392,362 shares of Wells Fargo common stock as of December 31, 1990. Defendant Reichardt is chairman of Wells Fargo's Executive Committee, which is authorized to supervise the general management and direction of the business affairs of Wells Fargo, and is a member of Wells Fargo Bank's Trust Committee which supervises the administration and proper exercise of the fiduciary powers of Wells Fargo Bank. As a result of his position, Defendant Reichardt had the ultimate responsibility for supplying data and determining final presentation of statements made to the investment community in the form of press releases and public filing by Wells Fargo, as well as the ultimate determination and review of Wells Fargo's loan portfolio, including assuring that proper financial controls were followed, that collateral was properly valued, and that such risks were properly assessed and reflected in the Company's financial statements.

22. Defendant Paul Hazen ("Hazen") is President and Chief Operating Officer of Wells Fargo. Hazen is a member of the Board of Directors of the Company. For 1990, Defendant Hazen received total cash and other compensation from Wells Fargo of at least $1,081,667. For the years 1988, 1989 and 1990, Defendant Hazen has received incentive based cash bonuses from Wells Fargo of at least $1,640,000. Defendant Hazen was the beneficial owner of 290,378 shares of Wells Fargo's common stock as of December 31, 1990. Defendant Hazen is a member of Wells Fargo's Executive Committee, and is chairman of Wells Fargo Bank's Trust Committee. As a result of his positions, Defendant Hazen had responsibility for the ultimate determination of and review of the loan portfolio of Wells Fargo including assuring that proper financial controls were followed, that collateral was properly valued, and that credit risks were properly assessed and reflected on Wells Fargo's financial statements.

23. Defendant Robert L. Joss ("Joss") is vice-chairman of Wells Fargo. For 1990, Defendant Joss received total cash and other compensation from Wells Fargo of at least $750,000. For the years 1988, 1989 and 1990, Defendant Joss has received incentive based cash bonuses from Wells Fargo of at least $1,015,000.

24. Defendant David M. Petrone ("Petrone") is vice-chairman of Wells Fargo. For 1990, Defendant Petrone received total cash and other compensation from Wells Fargo of at least $703,333. For the years 1988, 1989 and 1990, Defendant Petrone received incentive based cash bonuses from Wells Fargo of at least $965,000.

25. Defendant William F. Zuendt ("Zuendt") is vice-chairman of Wells Fargo. For the year 1990, Defendant Zuendt received total cash and other compensation from Wells Fargo of at least $753,333. For the years 1988, 1989 and 1990, Defendant Zuendt received incentive based cash bonuses from Wells Fargo of at least $1,045,000.

26. Defendant Clyde W. Ostler ("Ostler") is vice-chairman of Wells Fargo.

27. Defendant Stephen A. Enna ("Enna") is executive vice-president of Wells Fargo.

28. Defendant Rodney L. Jacobs ("Jacobs") is executive vice-president and chief financial officer of Wells Fargo.

29. Defendant Patrick W. Leahy ("Leahy") is executive vice-president of Wells Fargo.

30. Defendant Guy Rounsaville, Jr. ("Rounsaville") is executive vice-president, and chief counsel and secretary of Wells Fargo.

31. Defendants Reichardt, Hazen, Joss, Ostler, Petrone, Zuendt, Enna, Jacobs, Leahy and Rounsaville, shall be collectively referred to as the "Individual Defendants."

32. Each of the Individual Defendants is an executive of Wells Fargo and was therefore entitled to participate in one or more of the following Wells Fargo benefit plans:

(a) Wells Fargo's Incentive Pay Plan, under which all executives of Wells Fargo as a group received at least $6,731,332 in 1990;

(b) Wells Fargo's Tax Advantage Retirement under which all of the executives of Wells Fargo as a group received at least $416,126 in 1990;

(c) Wells Fargo's Employee Stock Purchase Plan;

(d) Wells Fargo's Executive Life Plan, which pays lump-sum benefits upon the death of a participant;

(e) Wells Fargo Executive Loan Plan, which entitles Wells Fargo executives to receive general purpose or mortgage loans at favorable interest rates, which in February of 1991 was as low as 6.96%, the balance of these loans as of December 31, 1990 was $4,708,879; and

(f) Wells Fargo's Equity Interest Plan, which grants certain executives options or restricted share rights which may be converted into Wells Fargo common stock, under which all of the executives of Wells Fargo as a group received options to purchase 349,000 shares of Wells Fargo stock, the net value of which was $5,124,793, as defined by market value less exercise price.

33. To properly discharge their duties and obligations, the Individual Defendants, and each of them, were required to exercise prudent supervision over the management and financial affairs of Wells Fargo. By virtue of this obligation, the Individual Defendants were required, among other things:

(a) To manage, conduct, supervise and direct the business and affairs of Wells Fargo in accordance with state and federal laws;

(b) To exercise reasonable control and supervision over the officers and employees of Wells Fargo;

(c) To exercise reasonable care in evaluation of the prudence and soundness of policies and practices proposed to be undertaken by Wells Fargo;

(d) To ensure that Wells Fargo did not engage in unsafe, imprudent or unsound practices and that Wells Fargo complied with all federal and state laws and regulations;

(e) To establish guidelines and policies adequately governing the structure and organization of the Company's operations;

(f) To establish guidelines and policies adequately governing the standards for credit approval, investment activities and the auditing process;

(g) To establish guidelines and policies adequately governing Wells Fargo's accounting practices and its investments;

(h) Not to violate, or knowingly permit any officer, director or employee of Wells Fargo to violate applicable federal laws, rules and regulations;

(i) To exercise reasonable control and supervision over the officers and employees of Wells Fargo;

(j) To maintain a proper division of authority and responsibility among the officers and directors of Wells Fargo so as to prevent the dominance of any officer or director in the conduct of the business and affairs of Wells Fargo;

(k) To exercise reasonable care in evaluation of the prudence and soundness of policies and practices proposed to be undertaken by Wells Fargo;

(l) To ensure that Wells Fargo did not engage in unsafe, imprudent or unsound practices and to become and remain informed as to how Wells Fargo was, in fact, operating;

(m) Upon receiving notice or information of an unsafe, imprudent or unsound practice, to make a reasonable investigation of the matter and to take steps to correct that condition or practice;

(n) To establish and maintain systematic and accurate books and records of the business and affairs of Wells Fargo and procedures for the reporting of the business and affairs to the Board of Directors and periodically to investigate, or cause independent investigation to be made of, the books and records;

(o) To maintain and implement an adequate and functioning system of internal financial, accounting and lending controls and management information systems, such that Wells Fargo's assets would be safeguarded, its financial statements and information would be accurately recorded and reported and corporate managers would be given prompt notice of serious problems or divergences so that risk to the corporation would be minimized; and

(p) To supervise the preparation and filing of any audited or unaudited financial statements, reports or other information required by law from Wells Fargo, to examine and evaluate any reports of examination, audits or other information required by federal or state law concerning the financial condition of Wells Fargo and to make full and accurate disclosure of all material facts concerning, *inter alia*, each of the subjects and duties set forth above.

CONSPIRACY, COMMON COURSE OF CONDUCT AND AIDING AND ABETTING

34. Prior to the beginning of the Class Period, the Defendants, and each of them, began a course of conduct which was designed to and did (i) deceive the investing public, including Plaintiffs and the other Class members, regarding Wells Fargo's business, markets, results of operations, financial condition and its future business prospects; (ii) conceal the Individual Defendants' gross mismanagement of Wells Fargo and the Defendants' falsification of Wells Fargo's financial statements; (iii) artificially inflate the market price of Wells Fargo common stock during the Class Period; (iv) inflate the compensation certain Defendants would receive as officers of Wells Fargo; and (v) cause Plaintiffs and other members of the Class to purchase Wells Fargo's common stock at inflated prices. In furtherance of this plan and course of conduct, the Defendants took the actions as herein set forth.

35. The Individual Defendants participated in the wrongdoing complained of herein in order to continue and prolong the image of Wells Fargo as a well-managed enterprise with sound lending procedures and vigorous credit review procedures which was achieving profitability and in order to conceal the adverse facts concerning the Company's markets, business, management, financial condition and future business and earnings prospects, so that they could (i) protect and enhance their executive positions and the substantial compensation and prestige they obtained thereby; (ii) enhance the value of their personal Wells Fargo securities holdings and options; and (iii) inflate the apparent profits of the Company in order to obtain

larger payments under Wells Fargo's incentive bonus compensation plan and/or individual performance discretionary bonuses.

36. The conspiracy, common enterprise and common course of conduct that commenced in or about March 1991 involved all of the Defendants named herein. The purpose and affect [sic] of the conspiracy, common enterprise and common course of conduct complained of was, *inter alia*, to inflate the market price of Wells Fargo's common stock in violation of the anti-fraud provisions of the federal, securities laws and statutory and common laws and obscure and delay the disclosure of the horrible results of Defendants' failure to (i) observe prudent lending practices; (ii) adequately monitor Wells Fargo's loan portfolio; and (iii) establish adequate loan loss reserves. The Defendants accomplished their conspiracy, common enterprise and common course of conduct by artificially inflating the price of Wells Fargo common stock for as long as possible through the issuance of the series of false and misleading annual and quarterly reports, financial statements, and press releases as particularized herein. Each Defendant was a direct, necessary and substantial participant in the conspiracy, common enterprise and common course of conduct complained of herein.

37. Each of the Defendants named herein aided and abetted and rendered substantial assistance in the accomplishment of the fraud complained of herein. In taking the action, as particularized herein, to aid and abet and substantially assist the commission of the fraud complained of, each Defendant acted with an awareness of the primary wrongdoing and realized that its/his conduct would substantially assist the accomplishment of that fraud and was aware of its/his overall contribution to and furtherance of the conspiracy, common enterprise and common course of conduct. Defendants' acts of aiding and abetting include, *inter alia*, all of the acts each of them are alleged to have committed in furtherance of the conspiracy, common enterprise and common course of conduct complained of above except those relating to the reaching of agreements or understanding sufficient to categorize their conduct as conspiratorial.

38. As members of the Board of Directors of Wells Fargo, the directors named herein as Defendants were themselves directly responsible for authorizing or permitting authorization of, or failing to monitor, the practices which resulted in the huge losses suffered by Wells Fargo as alleged herein. Each of them had knowledge of and actively participated in and approved of the wrongdoings alleged or abdicated his responsibilities with respect to these wrongdoings. The alleged acts of wrongdoing were committed outside of normal banking practices and subjected Wells Fargo to unreasonable risks of loss.

39. Each of the Individual Defendants is liable as a direct participant in, an aider and abettor of, and co-conspirator with respect to, the wrongs complained of herein. Each of the Individual Defendants reviewed or was aware of each of the alleged misleading reports and statements complained of herein at or about the time they were issued or circulated, knew of or recklessly disregarded their false and misleading nature and was in a position to control or influence the content of such reports or otherwise cause corrective/accurate disclosures to have been made.

40. All the Individual Defendants engaged in a conspiracy, common enterprise or common course of conduct, the purpose and effect of which was, *inter alia*, to artificially inflate and support the market price of Wells Fargo publicly-traded securities. The Individual Defendants accomplished their part of the conspiracy, common enterprise or common course of conduct by artificially inflating the price of Wells Fargo common stock in the public markets through the issuance of materially false and misleading reports filed with the SEC, annual and quarterly reports to shareholders, releases to the public and financial statements in each of these as particularized herein. Additionally, the Individual Defendants, because of their positions of control and authority as officers and/or directors of the Company, were able to and did control the conduct of Wells Fargo's business as well as the contents of the various annual and quarterly reports, press releases and the statements of the Company and financial statements in each of these. As officers and/or directors of a publicly-held company, the Individual Defendants had a duty to promptly disseminate accurate and truthful information with respect to the Company's opera-

tions, products, management, projections and forecasts, so that the market price of the Company's common stock would be based on truthful and accurate information.

CLASS ACTION ALLEGATIONS

41. This action is brought by Plaintiffs and the Class pursuant to Rules 23(a) and 23(b)(3) of the Federal Rules of Civil Procedure on behalf of all persons and entities who purchased the common stock of Wells Fargo during the period from March 5, 1991 through June 25, 1991, and were damaged thereby. Excluded from the Class are the Defendants, the members of Defendants' immediate families, any entity in which any of the Defendants has a controlling interest, any employees, officers or directors of any of the Defendants, and the legal representatives, heirs, successors and assignees of any of the Defendants.

42. A significant number of Wells Fargo shares were actively traded on NASDAQ, and the New York and Pacific Stock Exchanges, all effective national markets, during the Class Period. There are in excess of 30,000 shareholders of the some 50,000,000 shares of common stock of Wells Fargo which are concurrently issued and outstanding. The members of the Class are so numerous that individual joinder of all members is impracticable.

43. There are common questions of law and fact which predominate over any questions affecting only individual Class members. Among the common questions of law and fact are the following:

(a) Whether Defendants made material misrepresentations and omissions to the Class regarding the financial health of Wells Fargo;

(b) Whether Defendants acted willfully, recklessly or negligently in omitting and/or misrepresenting material facts;

(c) Whether Defendants' conduct violated federal securities laws, including §10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder; and relevant California state law:

(d) Whether the Company's reports to the SEC on Form 10-K and 10-Q, its reports to shareholders, and its other publicly filed and disseminated documents and other statements disseminated to the Class omitted and/or misrepresented material facts about the business and finances of the Company;

(e) Whether the market price of Wells Fargo's common stock was artificially inflated due to the conduct of Defendants, including the alleged non-disclosures and/or misrepresentations complained of here;

(f) Whether Defendants participated in and pursued the conspiracy and common course of conduct complained of here; and

(g) The extent of damages sustained by Plaintiffs and the Class, and the proper measure of damages.

44. The Individual and Representative Plaintiffs' claims are typical of the claims of the members of the Class. Plaintiffs are members of the Class they seek to represent in that they purchased shares of Wells Fargo common stock at an artificially inflated price within the Class Period, and were injured by the same wrongful conduct that injured the other members of the Class.

45. Plaintiffs will fairly and adequately protect the interests of the members of the Class. Plaintiffs have retained counsel who are experienced and competent in class action litigation under the federal securities laws. The Plaintiffs have no interest which are [sic] adverse or antagonistic to the interests of the Class.

46. Plaintiffs know of no difficulty that will be encountered in the management of this litigation that would preclude its maintenance as a class action.

47. The names and addresses of the records [sic] owners of Wells Fargo common stock purchased during the Class Period are available from Wells Fargo and/or Wells Fargo's transfer agent. Notice can be provided to such record owners, via first class mail, using techniques and a form of notice similar to those similarly and regularly employed in class actions arising under the Federal Securities laws.

48. A class action is superior to any other available method for the fair and efficient adjudication of this controversy. Because the damages suffered by individual Class members may be relatively small, the burden and expense make it impracticable for Class members to seek redress individually for the wrongs done to them. The management of this lawsuit as a class action presents far fewer management difficulties than individualized actions and provides the benefits of unitary adjudication, economy of scale and comprehensive supervision by a single court.

FACTUAL BACKGROUND

49. Defendant Wells Fargo, parent of Wells Fargo Bank, N.A. (the "Bank"), is a holding company engaged in the real estate and financial services business. Wells Fargo common stock is registered with the SEC pursuant to §12(b) of the Exchange Act and its common stock is listed and actively traded on NASDAQ and on the New York and Pacific Stock Exchanges in an efficient market. Wells Fargo has at least 50,000,000 shares of common stock outstanding held by approximately 30,000 owners of record.

50. Prior to the Class Period, Wells Fargo aggressively courted the business of promoters of leveraged buy-outs ("LBO's") and other similar transactions, as well as highly speculative real estate developers. Wells Fargo rapidly built a large portfolio of risky HLT Loans, as well as construction and development loans. These loans were particularly attractive to Wells Fargo, as they allowed the Company to immediately account for substantial amounts of up-front commitment and other fees.

51. Prior to and during the Class Period, Defendants witnessed a substantial deterioration of the quality of Wells Fargo's loan portfolio. This deterioration was most noticeable in Wells Fargo's HLT Loans and its real estate and commercial loans, which were, to a substantial degree, not fundamentally sound and prone to non-repayment in foreseeable and predictable economic downturns. During this time period, Defendants were aware of a national and local economic downturn, the weakening of Wells Fargo's local real estate portfolio and Wells Fargo's significant exposure in local real estate and development projects with questionable prospects for repayment. At no time prior to June 25, 1991 did Defendants reveal the extent of Wells Fargo's speculative lending activities and the resulting consequences.

52. Throughout the Class Period, Defendants also portrayed to the public that it was "business as usual" at Wells Fargo. In fact, Defendants knew, or were reckless in ignoring facts which should have made them know that Wells Fargo had granted numerous loans which presented unacceptable risks of non-payment and loss due to, *inter alia*, the substantial decline in its local real estate loan portfolio, the terms of the loans and/or the financial weakness of the borrowers. Moreover, despite their knowledge of the decline and signs of non-payment, Defendants also intentionally or, at a minimum, recklessly maintained inadequate reserves and established inadequate provisions for loan losses for Wells Fargo's HLT and real estate loans, all of which was intended to conceal from the investing public and the federal banking regulators how poorly Wells Fargo had been managed by the Individual Defendants and how badly its financial and operating condition had deteriorated.

53. Throughout the Class Period, Wells Fargo was in frequent telephonic and personal contact with stock market professionals, analysts, money managers, institutional investors and similar members of the professional investment community, in part through activities of various officers and directors who periodically (and at least monthly) provided information to gatherings of securities analysts to promote the Company and purportedly to inform the investment community of the current status and near and long-term prospects of the Company. At these presentations and in other formal and infor-

mal contacts, the Defendants consistently advised, stated and confirmed to analysts and other stock market professionals that Wells Fargo would achieve substantially increased revenues and earnings in 1991 and that Wells Fargo had accurately and adequately evaluated and valued non-performing assets in the Company's loan and real estate portfolios and established adequate loan loss reserves. There was no reasonable basis for these forecasts when made, and the true adverse facts about Wells Fargo's markets, asset values, level of non-performing assets, financial condition, and future business prospects, which were known to or recklessly disregarded by Defendants, contradicted the forecasts as made and made it very unlikely that such increased earnings would be achieved. These statements were materially false and misleading when made and operated to artificially inflate the market price of Wells Fargo common stock during the Class Period.

54. Under banking regulations, a highly-leveraged transaction is a financial transaction that exceeds $20 million and involves the buyout, acquisition or recapitalization of an existing business. In addition, the transaction at least doubles the Company's liabilities and results in a leveraged ratio of higher than 50%, or the transaction results in a leveraged ratio higher than 75%, or the transaction is designated a highly-leveraged transaction by a syndication agent. As of March 31, 1991, Wells Fargo had over $3.5 billion worth of HLTs.

55. Each quarter, a financial institution must maintain its loan loss reserves, and is required to add an appropriate provision for loan losses, which is necessary to maintain the reserves at an appropriate level consistent with the risk of loss actually faced. In determining the amount of the loan-loss provisions and reserves, a bank or holding company such as Wells Fargo is required to consider, *inter alia*, (i) the current trend of delinquencies; (ii) excessive loan renewals and extensions; (iii) the absence of current financial data related to borrowers and guarantors; (iv) the borrower's current condition, such as whether it is experiencing operating losses, marginal working capital, or inadequate cash flow; (v) loans secured by collateral that is not readily marketable or is susceptible to deterioration in realizable value; and (vi) loans in areas or businesses experiencing economic instability.

56. Depending on the risk associated with a particular transaction, the bank is required to set aside an appropriate amount of funds in its loan loss reserves to compensate for the high risk of such transactions. In the first quarter of 1991, Wells Fargo "set aside" only $85 million for loan losses.

57. Provisions for loan losses are to be recorded on a bank's financial statements, and were recorded on Wells Fargo's financial statements, as a direct charge to, and reduction from, net income, and, thus, earnings per share. Accordingly, Defendants knew that if they established the necessary and adequate provision for loan losses given Wells Fargo's risky real estate and HLT Loans, such disclosures would have had a substantial negative impact on Wells Fargo's earnings and on the Company's ability to comply with capital requirements imposed by the banking authorities. The Individual Defendants were also aware that if they truthfully described Wells Fargo's deteriorated financial position in regard to, *inter alia,* its sub-standard and high-risk HLT and real estate loans, their highly lucrative positions as officers and directors would be jeopardized and the market prices of Wells Fargo securities would also be negatively impacted. Such disclosures, if they had been made, would have at a minimum been an early warning sign that Wells Fargo was an extremely high-risk speculation and not "safe and stable" as portrayed by Defendants. Defendants made efforts to conceal the truth that would eventually be revealed on June 25, 1991: that Wells Fargo's financial condition and loan portfolio required massive additions to its loan loss reserves.

58. Prior to and during the Class Period, Defendants knew, or were reckless in disregarding facts which indicated that Wells Fargo's commercial, HLT and real estate loan portfolios were in serious distress and, consequently, that Wells Fargo's loan loss reserves, especially in connection with HLT and real estate development loans, were woefully inadequate and presented a misleading picture of the Company's true earnings. Had Defendants accurately reflected the poor quality of Wells Fargo's loan portfolio in its loan loss reserves, either no profits would have been reportable and a loss would have resulted or, to the extent there might have been profits, such profits would have been minimal. Nonetheless, Defendants intentionally or reck-

lessly withheld this information, in order to inflate the Company's earnings and enrich the Individual Defendants as a result of the Wells Fargo compensation plans.

59. As described above, prior to and during the Class Period, Wells Fargo aggressively courted the business of promoters of HLTs. As a result, Wells Fargo quickly built upon one of the largest portfolios of HLT Loans in the country. It was also one of California's largest sources of financing for speculative real estate development. When the promoters of HLTs and real estate developers began to experience financial difficulties and/or problems in repaying the loans prior to and at the beginning of the Class Period, Defendants were on notice that a substantial portion of Wells Fargo's outstanding HLT Loans and real estate loans were in jeopardy, particularly in light of the information that was available to the Individual Defendants as sophisticated officers and directors of this major bank holding company.

60. Defendants, however, did not disclose these facts nor did they establish adequate provisions for loan losses on these loans. Among the high-risk HLT Loans for which Defendants were on notice of these problems were, *inter alia*, Revco D.S., Insilco Corp., Charter Medical Corp., R.H. Macy & Co., Campeau Corp., Jim Walters Corp., Gaylord Container Corp., West Point Pepperell, Inc., and NWA, Inc.

61. To the extent Defendants reviewed the financial condition of the promoters of the HLT Loans, including those referred to in the preceding paragraph, the likelihood of non-payment on their loans, and the enormous risk associated with those loans through all or most of the Class Period, the Individual Defendants or their subordinates either did not critically examine or assess the adverse situation relating to these loans. It was not until concern over the banking regulators' examination of Wells Fargo in the spring of 1991 (through the Shared National Credit Regulatory Examination and otherwise) became public that the Individual Defendants caused management to critically review Wells Fargo's HLT Loans and determined that, in many of these loans, which were at all times speculative and highly

risky, the likelihood of default had increased dramatically. Although the borrowers' financial condition had greatly deteriorated prior to the commencement of the Class Period, Defendants still failed to disclose to the public and regulators the fact of this deterioration.

62. Prior to the Class Period, Wells Fargo made numerous speculative loans which, in the aggregate constituted a material portion of Wells Fargo's total loan portfolio. A substantial portion of these loans made little or no economic sense for Wells Fargo in light of the prevailing market and other conditions as described here. As a result, Defendants were aware, or were reckless in disregarding facts which indicated that, at the time these loans were made, it was highly probable that these loans would go into default. Even for those loans made well before the Class Period, Defendants knew, at least by the commencement of the Class Period, that it was likely that these loans would become non-performing (if they were not already non-performing) and require the establishment of substantial additional loan loss reserves. Despite their knowledge of these facts, Defendants intentionally and/or recklessly established inadequate loan loss reserves for these HLT Loans and real estate loans, all of which artificially inflated Wells Fargo's reported earnings, assets and net worth, by material amounts.

63. The Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Reserve Board, and the Office of Thrift Supervision regularly promulgates instructions and regulations regarding the operations of financial institutions such as Wells Fargo. Throughout the Class Period, Wells Fargo intentionally or recklessly disregarded certain of these instructions, including, *inter alia,* instructions regarding public disclosures.

64. On January 25, 1991, the Office of the Comptroller of the Currency issued Banking Bulletin No. 91-05. The Banking Bulletin was issued to "encourage national banks to consider providing more detailed information in public disclosures about non-accrual loans." The January 25, 1991 Banking Bulletin provided a sample disclosure form which provided for, *inter alia,* full disclosure of information regarding loans placed on non-accrual status.

65. On March 1, 1991, the Office of the Comptroller of the currency, the Federal Deposit Insurance Corporation, the Federal Reserve Board, and the Office of Thrift Supervision issued a joint agency policy statement ("Joint Statement") concerning non-accrual assets, and highly leveraged transactions. The four agencies, which supervise over 12,000 commercial banks and 2,400 thrift institutions, indicated that the purposes underlying regulatory and accounting policies were to "encourage disclosure about the condition of" financial institutions' loan portfolios. The guidelines and statements were released, *inter alia*, to "encourage enhanced disclosure to the public" and "to better assure sound assessments of the value of real estate."

66. The four federal regulatory agencies fully supported the Office of the Comptroller of the Currency's previous Banking Bulletin (Banking Bulletin No. 91-05) issued on January 25, 1991. The Joint Statement went on to indicate that "*enhanced disclosure will help ensure that the public is better informed about the nature of institutions' portfolios.*"

67. With respect to enhanced disclosure, the Joint Statement indicated that "the simple total of such [non-accrual] loans on an institution's books may not be a good indicator of the institution's financial position." The federal regulatory agencies issuing the statement fully supported the disclosure of the type requested by the Office of the Comptroller of the Currency in the January 25, 1991 Bulletin.

68. With respect to valuation of real estate loans, the Joint Statement indicated that "it is important that valuation techniques reflect *not only existing market conditions, but also reasonable expectations of the property's performance in the market over time.* The federal regulatory agencies are reiterating their policy on the assessment of real estate values and the establishment of loan loss reserves." The statement went on to warn that "the basic thrust of this guidance is to ensure that income property loans not be assessed solely on the basis of liquidation values but also on the income-producing capacities of the properties over time. *Supervisory evaluations should take into account*

the lack of liquidity and cyclical nature of real estate markets and temporary imbalances in the supply and demand for real estate that may occur."

69. With respect to multiple loans to one borrower, the Joint Statement went on to require that when one loan to a borrower is placed on non-accrual status, the institution is required to evaluate its other extensions of credits to the one borrower to determine whether one or more of the other assets must also be placed on non-accrual status.

70. Adopting the policy discussed in Banking Bulletin No. 91-05, the Joint Statement stated that the current public disclosure about non-accrual assets, generally limited to the total amount of non-accrual assets, interest income and interest foregone, is insufficient to fully disclose the impact that non-accrual assets have on earnings and financial conditions of a particular financial institution. Accordingly, the Joint Statement suggested that these institutions make additional disclosures about non-accrual assets "in their annual reports." The Joint Statement provided a sample disclosure statement, which listed specific, important and material information regarding, past due substantial performance, limited performance, principal or interest in doubt, and the like. This was the adoption of the sample disclosure form set forth in Banking Bulletin No. 91-05.

71. With respect to HLTs, the Joint Statement indicated that once an individual credit is designated as an HLT, all current outstanding and future obligations by the same borrower are considered HLT Loans.

72. On May 20, 1991, the Office of the Comptroller of the Currency issued Banking Bulletin No. 91-19 regarding non-accrual loans. Banking Bulletin No. 91-19 specifically stated that a bank with more than one loan to a borrower must reevaluate *all* loans to the borrower if any loan to that same borrower is placed on non-accrual status. The Banking Bulletin stated, "in summary, when a bank places one loan to a borrower on non-accrual status, a bank should reevaluate" whether the borrower's other loans should also be placed on non-accrual.

73. With respect to payments for non-accrual loans, the Office of the Comptroller of the Currency indicated that, if repayment of principal is not expected, payments received should be applied to the principal "to the extent necessary to restore the expectations of alternate collectibility." The loans should be placed on non-accrual status and payments should be made to reduce loan balance. This also requires non-accrual status for "all partially charged-off loans." The Banking Bulletin indicated that a loan is non-accrual when the borrower is unable to pay principal and interest when due. The Banking Bulletin also stated that "under existing regulatory policy, when a bank records a partial charge-off on a loan, it cannot continue to accrue interest income on that loan."

PUBLIC STATEMENTS AND REGULATORY FILINGS CONTAINING MISREPRESENTATIONS AND OMISSIONS OF MATERIAL FACT

74. During the Class Period, Defendants made public statements which were designed to conceal the facts set forth above, namely that Wells Fargo was experiencing serious payment problems on its HLT Loans and real estate loans, or was anticipating significant losses as a result of its substantial portfolio of HLT Loans, real estate construction and mortgage loans from at least the commencement of the Class Period. Despite knowledge of Wells Fargo's deteriorating loan portfolio, and the regulatory agencies' concern with proper accounting for loans placed on non-accrual status, Defendants made the statements detailed below concerning the purported actual and expected financial condition and performance of Wells Fargo. These statements were materially false and misleading in that they misstated and omitted to state material facts concerning the then-existing financial condition and loan portfolio of the Company and were made as a means to reassure the investment community that Wells Fargo was a conservative, growing institution with high asset quality, despite the ever-mounting deterioration of its condition caused by, *inter alia*, the HLT Loans, the speculative real estate ventures, and other high-risk loans made by Wells Fargo.

75. On or about March 5, 1991, in its 1990 Annual Report, Wells Fargo reported its net income for the fourth quarter and the full year of 1990. In the 1990 Annual Report, Defendants reassured the investing public:

> The year 1990 was marked by the threat of war in the Persian Gulf, a faltering economy and a continuous stream of bad news affecting the nation's financial services industry.
>
> In these unsettled times, investor concerns about what lay ahead for Wells Fargo and the California economy largely overshadowed the Company's steady financial performance.
>
> Net income for the year rose 18%, to $711.5 million. Earnings per common share were $13.39, an increase of 22% in comparison with last year's $11.02 per share.
>
> * * *
>
> Defensive actions — *redoubling surveillance of our real estate and corporate loan portfolios,* working out arrangements with delinquent borrowers, trimming back corporate and real estate banking activities, increasing loan loss reserves, and strengthening the Company's capital base — occupied an increasingly important place in our day-to-day agendas.
>
> * * *
>
> With the bulk of its loans and practically all of its deposits concentrated in California, Wells Fargo Bank has been a major contributor to — and beneficiary of — the state's economic growth.
>
> * * *
>
> *In short, we remain optimistic about California's prospects — and we still believe that our sharply focused regional marketing strategy is right for Wells Fargo. Over the years Wells Fargo has adopted a number of lending practices, pricing policies and credit standards designed to compensate for, and partly offset, the risks inherent in banking real estate and corporate credits.* These practices have worked well for us in the past, and *we believe they are especially appropriate to today's relatively high-risk banking environment.*

* * *

> Over the years Wells Fargo has adopted a number of lending practices, pricing policies and credit standards designed to compensate for, and partly offset, the risks inherent in banking real estate and corporate credits. These practices have worked well for us in the past, and we believe they are especially appropriate to today's relatively high-risk banking environment.
>
> But in the final analysis, whatever success we've had in corporate and real estate lending is due to two things: good customers and a well-seasoned team of senior lending officers.

* * *

> Among other things, experience has taught us to anticipate and react quickly to potential problems — and to recognize small problems before they become big ones. It has also taught us to place as much faith in our analysis of our borrowers' integrity and their ability to pay as in the value of their collateral.

76. Against this backdrop of calm reassurance, Defendants further stated with respect to Wells Fargo's HLT Loans in the Company's 1990 Annual Report:

> During the 1980s, Wells Fargo's Corporate Banking Group assisted in financing the restructuring, acquisition or buyout of slightly more than one hundred American corporations. Typically, Wells Fargo acted as lead banker and senior lender in these highly leveraged transactions (HLTs), providing secured term loans with average maturities of five to seven years. Normally, repayment schedules were based on reasonable projections of cash flow from operations, rather than the sale of corporate assets.

* * *

> The risks related to our HLT portfolio differ in two significant respects from those involved in real estate lending. First, the HLT portfolio is widely diversified, both geographically and by industry. Second, our experience in this type of lending has not been tested by recession. These differences make it more difficult to anticipate how the HLTs

> as a group will perform over the next 12 months. All we can say with certainty is that *we will be exercising even more than our customary diligence in managing our HLTs as well as all other segments of our loan portfolio in coming months.*

77. With respect to Wells Fargo's HLT Loan portfolio, Defendants stated in a table appearing at page 16 of the 1990 Annual Report:

> The Company believes at the present time that these loans are substantially secured by the assets of the borrowers. In addition, at December 31, 1990 and 1989, senior HLT loans past due 90 days and still accruing were $8 million and $209 million, respectively. There were no HLT loans on restructured status and there was no ORE resulting from HLT loans at December 31, 1990 and 1989. Senior HLT loans of $36 million and $30 million were charged off in 1990 and 1989, respectively. During an economic downturn or a sustained period of rising interest rates, HLT borrowers may experience a decrease in their financial performance greater than that of non-HLT borrowers.

78. With respect to other than HLT Loans, Defendants supplied numerous charts and tables, none of which warned the investing public of the full extent of the risks inherent there. Further, on page 18 of the 1990 Annual Report, Defendants advised shareholders that substantially all of Wells Fargo's commercial loan net charge-offs in 1990 were related to HLTs, implying that the Company's remaining loans were quite healthy. Defendants went on to say, without basis in fact, that:

> The Company's determination of the level of the allowance, and correspondingly, the provision for loan losses rests upon various judgments and assumptions including, but not limited to, general economic conditions, loan portfolio composition and prior loan loss experience. The Company considers the allowance for loan losses of $885.4 million adequate to cover losses inherent in loans; commercial, real estate and other loan commitments; and stand-by letters of credit as of December 31, 1990.

79. Such statements and others were utterly deceptive in that they concealed the fact that many of the Company's HLT Loans and major real estate development loans were already high-risk, that the

borrowers already faced serious risk of failure of timely repayment, and that the Office of the Comptroller of the Currency (and other regulatory agencies) had issued regulations requiring banks, such as Wells Fargo, to increase loan loss reserves, re-evaluate loans and to place certain loans on non-accrual status, when appropriate.

80. On April 16, 1991, and in subsequent SEC filings in the first quarter Report to Shareholders, Wells Fargo reported that its earnings per share on the first quarter of 1991 were $2.86 on net income of $152 million. Wells Fargo stated it had made a loan loss provision of $85 million and represented that those financial results included all adjustments and provisions necessary for fair presentation of its results in conformity with Generally Accepted Accounting Principles ("GAAP"). Wells Fargo's first quarter earnings as reported were well in excess of analysts' expectations, due, in large part, to the modest size of the loan loss reserve provision. As a result, Wells Fargo stock jumped over $4 per share to over $76 and continued to increase to over $90 per share during the balance of the Class Period.

JUNE ANNOUNCEMENTS

81. In a June 10, 1991 article in *Barrons* Financial Weekly, the Company dismissed the claim that Wells Fargo might face a possible increase in non-performing real estate loans for the second quarter of 1991. Rather, the Company noted that for the past 16 years, Wells Fargo averaged only "0.13" of a percentage point in real estate lending losses.

82. On June 18, 1991, Wells Fargo announced that its Board had declared a regular quarterly dividend of $1.00 per share. On June 24, 1991, Wells Fargo stock fell sharply. In response to inquiries, Wells Fargo stated that "*it knew of no reason to explain*" the drop in its stock prices.

83. Despite the promising picture painted by Wells Fargo and the Individual Defendants, on June 25, 1991, Wells Fargo requested that the New York Stock Exchange delay the opening of trading of its stock, pending an announcement to be made by Wells Fargo.

84. On June 25, 1991, Wells Fargo announced that it would increase its reserves for loan losses in the second quarter of 1991. The Company announced that it expected to have a second quarter provision for loan losses of approximately $350 million. This loan loss reserve was approximately four times the $85 million loan loss reserve for the first quarter of 1991. This increase raised the total loan loss reserved to a total of over $1 billion.

85. The Company also announced that it expected actual loan losses in the second quarter to be approximately $180 million. This amount was over two and one-half times the $67 million in loan losses reported for the first quarter of 1991.

86. Due to the increase in previously unannounced loan losses, Wells Fargo estimated that its net income for the second quarter of 1991 would be approximately $15 million or approximately 20 cents per common share. Wells Fargo also announced that it would be placing $40 million of commercial loans on a "non-accrual" basis. Wells Fargo's announcement of 20 cents per share was based on a formerly undisclosed $35 million write-off for losses due to Wells Fargo's investments in HLTs and bad loans. Prior to the announcement it was widely believed that Wells Fargo's net income would be much greater.

87. The Company also announced that approximately half of the loans placed on non-accrual were HLTs.

88. As a result of this public disclosure of previously withheld information, the value of Wells Fargo stock plummeted: after the announcement, the stock declined from the previous high of $97 per share to $74 per share.

89. The reasons for Wells Fargo's downturn were known, or should have been known, to Defendants at the commencement of, and throughout, the Class Period, and were wrongfully and illegally withheld from Plaintiffs and the Class.

90. By reason of the foregoing uniform false and misleading statements, and concealments and non-disclosures, the market price of

Wells Fargo stock was artificially inflated at all times during the Class Period.

91. Due to the Defendants' false statements about Wells Fargo's business and earnings, Wells Fargo's common stock traded at artificially inflated prices during the Class Period, prior to the disclosure of the previously concealed adverse information about Wells Fargo. As a result of these false and misleading statements and Defendants' failure to reveal the full truth about Wells Fargo, Wells Fargo common stock traded during the entire Class Period at artificially inflated prices until on or after June 25, 1991, when full disclosure was finally made. Plaintiffs and the members of the Class purchased or otherwise acquired the common stock of Wells Fargo during the Class Period in reliance upon the integrity of the marketplace and Defendants' false statements including Wells Fargo's false financial statements, all of which were known to Defendants, and were damaged thereby.

92. As a result of the dissemination of the aforementioned false and misleading financial statements, annual and quarterly reports to shareholders and the SEC, press releases and other public communications, the market prices of Wells Fargo's common stock were artificially inflated throughout the Class Period. In ignorance of the adverse facts concerning Wells Fargo's financial condition, which were concealed by Defendants, Plaintiffs and members of the Class purchased or otherwise acquired the common stock of Wells Fargo at artificially high prices, relying upon the integrity of the market, and were damaged thereby. Had Plaintiff and the members of the Class known of the materially adverse information not disclosed by Defendants, they would not have purchased or acquired Wells Fargo common stock and other securities at the artificially inflated prices they did.

UNDISCLOSED ADVERSE INFORMATION

93. The public announcements, financial statements and reports, SEC filings, shareholder reports and analysts' reports based thereon were each materially false and misleading. Prior to June 25, 1991, Defendants portrayed Wells Fargo as a very successful company

whose future prospects of profitable growth would be and continued to be enhanced, through the Company's capable management, excellent lending controls and credit monitoring procedures, high-quality loan portfolio and ability to control its level of non-performing assets.

94. In violation of applicable SEC rules and regulations, these public statements failed to disclose "known trends or uncertainties," *i.e.*, the material adverse information stated below, that Defendants knew would "have a material ... unfavorable impact on net sales or revenues or income from continuing operations," and also failed to disclose "material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition." Regulation S-K, Item 303(a)(3)(ii) and Instruction 3; 17 C.F.R. §229.303(a)(3)(ii).

95. Prior to and during the Class Period, Wells Fargo failed to comply, and failed to disclose its non-compliance, with the Office of the Comptroller of the Currency's policy statements and guidelines regarding, *inter alia*, (1) valuation of real estate loans; (2) recognizing non-performing loans; (3) enhanced public disclosure of non-accrual loans, and (4) evaluation of a single borrower's total extensions of credit when one loan to the borrower is placed on non-accrual status.

96. In addition, Wells Fargo failed to disclose the impact compliance or non-compliance with the Office of the Comptroller of the Currency's policy statements and guidelines would have upon the Company's earnings and profits. Specifically, Wells Fargo omitted to disclose that the Office of the Comptroller of the Currency's policies regarding HLTs, the determination of non-accrual status, evaluation of real estate loans and evaluation of all loans to a single borrower would dramatically decrease the Company's earnings for 1991.

97. The foregoing representations were each false and misleading at the time they were made, in that these statements concealed and failed to disclose, *inter alia*, the following adverse information con-

cerning Wells Fargo which was necessary to make the representations not misleading:

(a) That in order to conceal its growing amount of problem or non-performing loans and the dangers posed to Wells Fargo thereby, and to permit Wells Fargo to continue to falsely report large and increasing earnings, Wells Fargo failed to properly classify loans as problem or non-performing loans and thereby avoided establishing material amounts (over $350 million) of reserves for possible loan losses, which reserves were required in order to fully and accurately present Wells Fargo's actual financial results in conformity with GAAP and Regulatory Accounting Principles ("RAP");

(b) That Wells Fargo's first Quarter 1991 financial statements overstated Wells Fargo's assets, net income, earnings per share and stockholders' equity by material amounts because the Company failed to make timely and appropriate writedowns or establish reserves for likely losses on loans made by it;

(c) That Wells Fargo's non-performing assets and its reserves for possible loan losses were understated by at least $400 million and $350 million, respectively, due to the defaults on and doubtful collectibility of many of its loans, and that the earnings and stockholders' equity of Wells Fargo were correspondingly overstated;

(d) That because of Wells Fargo's undisclosed and understated non-performing loans and inadequate loan loss reserves, Wells Fargo's capital position was not nearly as strong as represented;

(e) That Wells Fargo was not fairly presenting or reporting its results from operations and its financial statements in conformity with GAAP and RAP, in that Wells Fargo's financial figures for the first quarter of 1991:

(i) Overstated income, assets and net worth as a result of Wells Fargo's failure to provide adequate reserves for losses on loans of doubtful collectibility;

(ii) Overstated income because interest income was being improperly accrued on non-performing loans and because loan origination fees were being recognized on loans that were uncreditworthy and did not meet Wells Fargo's lending standards or other prudent lending standards; and

(iii) Overstated retained earnings by the amount of income overstated and for the same reasons;

(f) That Wells Fargo lacked adequate internal financial and accounting controls and management information systems necessary to ensure the integrity of its assets and its resulting financial statements such that all assets, revenue and income from transactions recorded on Wells Fargo's books were reasonably expected to be realized and were not, in fact, fictitious or illusory;

(g) That Wells Fargo did not have management information systems or financial and accounting controls adequate for management to monitor, determine or accurately forecast the financial performance of the Company or evaluate the status of its loan portfolio on a timely basis;

(h) That because of the internal pressures at Wells Fargo generated from the top executive officers of Wells Fargo to report strong first quarter earnings and thus to "squeeze" short sellers of Wells Fargo stock and force the stock price up and then to purchase stock to "cover" their short position, Defendants falsified Wells Fargo's first quarter results to make Wells Fargo look far more profitable than it really was;

(i) That the quality and collectibility of Wells Fargo's loan portfolio had deteriorated significantly, largely because of the problems and actions set forth above. Unlike the Bank's traditional lending activities which involved California residential and other real estate loans, it had made over $4 billion in highly leveraged transaction loans without adequate evaluation or review of (i) the borrower's creditworthiness to determine if the borrower met Wells Fargo's standards, (ii) the adequacy or valuation of the collateral for the loans,

and (iii) the adequacy of the credit or loan documentation or its compliance with applicable state and federal regulations;

(j) That Wells Fargo's loan portfolio included at least $400 million of non-performing loans which were not timely accounted for or disclosed as such by Wells Fargo;

(k) That in order to conceal the growing amount of problem loans and the dangers posed to Wells Fargo thereby, and in order to permit Wells Fargo to continue to report earnings growth, Wells Fargo failed to properly classify loans as non-performing loans, and thereby avoided establishing material amounts of reserves for possible loan losses which were required in order to fairly and accurately present Wells Fargo's financial results, by granting unjustified maturity extensions, rate concessions and loan rollovers which were not in accord with standard practices and were not justified by the creditworthiness, current financial condition and loan performance of the borrowers;

(l) That Defendants authorized, caused or permitted Wells Fargo to make a large number of low-quality, HLT Loans, in part because its lending control and credit administration systems were inadequate to ensure proper collateralization of loans, proper valuation of collateral, compliance with Wells Fargo's documentation and lending procedures and prompt identification of problem loans and provision for their special handling and monitoring;

(m) That Defendants authorized, caused or permitted Wells Fargo to engage in an overly aggressive commercial lending program by which Wells Fargo made a significant volume of HLT Loans which Defendants knew or recklessly disregarded were of a substantially higher risk character than Wells Fargo's traditional activities and, thus, would likely result in major losses downstream;

(n) That Defendants caused or permitted the Bank repeatedly to violate 12 C.F.R. §563.161(a), requiring federal bank associations to "maintain safe and sound management" and to "pursue financial policies that are safe and consistent with ... the purposes of

federal savings associations and are appropriate to their respective types of operations";

(o) That in contravention of the rules, regulations and policies of the Office of the Comptroller of the Currency, Wells Fargo failed to properly: (i) place certain loans on non-accrual status; (ii) make additional and adequate disclosures about non-accrual loans in its annual reports and other publicly disseminated documents; (iii) evaluate real estate loans based on the ability of the collateral to generate adequate cash flow; and (iv) place multiple loans to one borrower in non-accrual status when one loan to the borrower is placed on non-accrual status;

(p) That a preliminary report of the Shared National Credit Regulatory Examination of Wells Fargo required the Company to increase its loan-loss reserves for loans placed on non-accrual status;

(q) That in contravention of the regulations promulgated by the SEC under the Exchange Act, specifically Item 303 of Regulation S-K, Defendants failed to report known trends and uncertainties regarding Wells Fargo's earnings, its loss reserves for loans and real estate, and its prospects for compliance with federal capital requirements;

(r) That, contrary to the Company's statements in its public reports that, *inter alia*, its financial statements had been prepared in conformity with GAAP and RAP and the rules and regulations of the SEC and fairly presented the Company's financial position, each of Wells Fargo's financial statements that was publicly disseminated during the Class Period in the Company's 1990 Annual Report and Quarterly Reports as of March 31, 1991, and Form 10-K and otherwise were false and misleading, in that such financial statements were not prepared in conformity with GAAP or RAP, were not prepared pursuant to the rules and regulations of the SEC, and did not reflect all adjustments necessary to present fairly the financial position, results of operations and changes in the financial position of Wells Fargo for the period or periods presented;

(s) That Wells Fargo's previously referenced financial statements violated the following GAAP principles, among others:

(i) The principle of fair presentation ("presents fairly") was violated. Statement No. 4 of the Accounting Principles Board ("APB Nos.") 4-109, 138, 189;

(ii) The principle of adequacy and fairness of disclosure was violated. APB Nos. 4-81, 106, 189, 199;

(iii) The principle of materiality concerning information that is significant enough to affect evaluations or decisions was violated. APB Nos. 4-25, 128;

(iv) The principle that the financial information presented should be complete was violated. APB Nos. 4-23, 94, 106;

(v) The principle that a conservative approach providing early recognition of unfavorable events and providing for the preservation and protection of shareholders and Company interest was violated. APB Nos. 4-28, 35, 171;

(vi) The principle that the substance of transactions rather than form should be reflected was violated. APB Nos. 4-25, 35, 127;

(vii) The principle that informed judgment based on background and knowledge should be applied was violated. APB Nos. 4-25, 35, 124, 173, 174;

(viii) The principle that items included in the financial statements be reliably corroborated by outside evidence (verifiability) was violated. APB Nos. 4-25, 35, 90;

(ix) The principle that the financial statements contain and disclose relevant, understandable and timely information for the economic decisions of the user was violated. APB Nos. 4-23, 88, 89, 92;

(x) The principle that the financial statements provide reliable financial information about the enterprise for the economic decisions of the user was violated. APB Nos. 4-77, 78, 107, 108;

(xi) The principles violated above are incorporated into the violation of the principle concerning the information contained in and disclosed, or not disclosed in, income statements. APB Nos. 4-23, 172;

(xii) Additionally, the principle that losses be accrued for when a loss contingency exists was violated. Statement of Financial Accounting Standards No. 5 (Accounting for Contingencies); and

(t) That federal regulators contemplated ordering Wells Fargo to increase its reserves for a number of loans.

ROLES AND ACTIVITIES OF OFFICER AND DIRECTOR DEFENDANTS

98. Defendants Reichardt and Hazen ("Director Defendants"), as members of the Company Board of Directors, are responsible for, participated in, conspired to bring about or aided and abetted the fraud complained of herein. Wells Fargo's Board of Directors operated as a collective entity through periodic meetings held either in person or telephonically where the Board of Directors operated as a collective entity through periodic meetings held either in person or telephonically where the Board discussed matters affecting Wells Fargo and its business and reached collective and consensual decisions as to what action to take. The members of the Board also received similar, if not identical, information from Wells Fargo executives and written reports from Wells Fargo's employees and management relating to the Company's business, including internal, periodic (including monthly) financial statements and official data and reports in advance of, at and subsequent to Board meetings in connection therewith. Corporate business of Wells Fargo at the Board level was conducted through formal resolutions passed by the directors acting collectively as is reflected in the minutes of the Wells Fargo Board of Directors. In addition, the Wells Fargo Board of Directors acted col-

lectively to issue the Form 10-K for the year ended December 31, 1990, as well as Wells Fargo's Annual Report to shareholders and quarterly reports to shareholders and the SEC for the quarter ended March 30, 1991, which reports were presented to and approved by the Board either before their issuance or shortly thereafter and, in the case of the Form 10-K, was signed by each of the directors or his duly authorized representative. Thus, because Wells Fargo's Board acted as a unit, conducted Wells Fargo's business pursuant to consensual agreements and formal resolutions as a Board, and received collectively the same information about Wells Fargo's financial condition and business prospects at or about the same time, it is appropriate to treat the members of the Board, both inside and outside directors, as a unit for pleading purposes.

99. With respect to Defendants Reichardt, Hazen, Joss, Ostler, Petrone, Zuendt, Enna, Jacobs, Leahy and Rounsaville ("Executive Officer Defendants"), each were involved in the day-to-day operations and management of the Company, and directly participated, through their respective executive positions, in the fraud alleged herein. Executive Officer Defendants Reichardt, Hazen, Joss, Ostler, Petrone, Zuendt, Enna, Jacobs, Leahy and Rounsaville were aware of the internal operations of Wells Fargo, including the fraudulent conduct described herein. Each of the Executive Officers reviewed or were [sic] aware of each of the alleged misleading reports and statements complained of herein at or about the time they were issued or circulated, knew of or recklessly disregarded their false and misleading nature and was in a position to control or influence the content of such reports or otherwise cause corrective/accurate disclosures to have been made.

100. Wells Fargo's Executive Officer Defendants operated as a collective entity through periodic meetings held either in person or telephonically where the Executive Officers operated as a collective entity through periodic meetings held either in person or telephonically where the Executive Officers discussed matters affecting Wells Fargo and its business and reached collective and consensual decisions as to what action to take. The Executive Officer Defendants also received similar, if not identical, information from Wells Fargo's

Board of Directors and written reports from Wells Fargo's employees and management relating to the Company's business, including internal, periodic (including monthly) financial statements and official data and reports in advance of, at and subsequent to meetings in connection therewith. Corporate business of Wells Fargo at the Executive level was conducted through formal resolutions passed by the directors acting collectively as is reflected in the minutes of the Wells Fargo Executive Officers. In addition, the Wells Fargo Executive Officers acted collectively to issue the Form 10-K for the year ended December 31, 1990, as well as Wells Fargo's Annual Report to shareholders and quarterly reports to shareholders and the SEC for the quarter ended March 30, 1991, which reports were presented to and approved by the Executive Officers either before their issuance or shortly thereafter and, in the case of the Form 10-K, was signed by each of the Executive Officers or his or her duly authorized representative. Thus, because Wells Fargo's Executive Officer Defendants acted as a unit, conducted Wells Fargo's business pursuant to consensual agreements and formal resolutions as Officers, and received collectively the same information about Wells Fargo's financial condition and business prospects at or about the same time, it is appropriate to treat the Executive Officers as a unit for pleading purposes.

101. The Individual Defendants, and each of them, breached their duties by their conduct, including, but not limited to, those acts and omissions outlined above and in addition:

(a) They caused or permitted Wells Fargo repeatedly to violate 12 C.F.R. §563.161(a), requiring federal banks associations to "maintain safe and sound management" and to "pursue financial policies that are safe and consistent with ... the purposes of federal savings associations and are appropriate to their respective types of operations";

(b) They further caused or permitted Wells Fargo to conduct its business in an unsafe, imprudent and dangerous manner by pursuing unsound practices including those specified herein and the concealment of such practices;

(c) They caused or permitted Wells Fargo to operate and report its financial information in a manner which was deceptive, misleading and contrary to GAAP, which overstated Wells Fargo's net worth and earnings and which concealed and minimized the size and true severity of the financial problems of Wells Fargo;

(d) They failed to institute guidelines or policies to prevent the acquisition of loans and other assets which did not meet accepted banking standards, and failed to establish internal controls sufficient to maintain asset quality; and

(e) They failed to terminate or substantially modify compensation programs which encouraged officers to generate loan and investment volume without sufficient regard for quality and stability.

102. In committing the wrongs complained of herein, the Defendants have caused Wells Fargo to repeatedly violate, the [sic] have themselves repeatedly violated federal law, including the federal securities laws, statutes and regulations relating to the operation of insured federal institutions and other applicable laws and regulations. Defendants have done this by causing Wells Fargo to violate applicable banking regulations and reporting requirements, as well as the internal controls, reporting and financial statement requirements of the federal securities laws.

103. In order to facilitate and to attempt to conceal their wrongdoing, the Officer and Director Defendants have caused or permitted Wells Fargo to maintain an inadequate system of internal financial and accounting controls such that Wells Fargo's assets have not been reasonably safeguarded against loss. Such conduct permitted the Individual Defendants, *inter alia*, to cause Wells Fargo to publicly report apparent profitable growth due to excellent controls and good management while, in fact, the Individual Defendants were squandering Wells Fargo's funds on hundreds of millions of dollars in bad loans on which Wells Fargo has suffered huge losses. In connection with the wrongdoing alleged herein these Defendants have caused and/or permitted their subordinates at Wells Fargo to make false and misleading and materially inaccurate entries in Wells Fargo's books

and records to disguise the nature of these loans and the losses on them.

FIRST CLAIM FOR RELIEF

(Sections 10(b) and 20 of the Securities Exchange Act of 1934, and Rule l0b-5 promulgated thereunder)

104. Plaintiffs reallege and incorporate paragraphs 1 through 103 above, as if set forth fully here.

105. Plaintiffs assert this First Claim for Relief individually and on behalf of all members of the Plaintiff Class against all Defendants for violations of §10(b) of the Exchange Act, 15 U.S.C. §78j(b), Rule 10b-5 promulgated thereunder, 17 C.F.R. §240.10b-5, §20 of the Exchange Act.

106. During the Class Period, Defendants, severally and in concert, directly and indirectly, participated, aided and abetted one another, and conspired with one another to participate and to aid and abet one another in a continuous course of conduct in connection with the purchase of securities in violation of §10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and by use of mails and other means and instruments of transportation and communications in interstate commerce: (a) employed manipulative devices, schemes and artifices to defraud Plaintiffs and members of the Plaintiff Class; (b) made untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in acts, practices and a course of business that operated as a fraud or deceit upon Plaintiffs and the Class in connection with their purchases of Wells Fargo common stock.

107. By reason of their stock ownership, their influence over substantial or controlling stockholders or their membership on the Wells Fargo's Board of Directors and positions as executive officers of the Company, the Individual Defendants were each controlling persons of Wells Fargo within the meaning of §20 of the Exchange Act throughout the Class Period and had the power and influence to

cause, and did cause, Wells Fargo to engage in the unlawful conduct complained of herein. Because of their Board membership and/or executive and managerial positions with Wells Fargo, each of the Individual Defendants had access to the adverse non-public information about Wells Fargo's business, finances and future business prospects via access to internal corporate documents, conversations and connections with corporate officers and employees, attendance at Board meetings and committees thereof and via reports and other information provided to them in connection therewith. Each of the Individual Defendants reviewed or was aware of each of the alleged misleading reports and statements complained of herein at or about the time they were issued or circulated, knew of or recklessly disregarded their false and misleading nature and was in a position to control or influence the content of such reports or otherwise cause corrective/accurate disclosures to have been made.

108. This claim for relief is brought against each of the Defendants here as a primary violator, control person aider and abettor and co-conspirator. The Individual Defendants are liable as primary violators and aiders and abettors by virtue of their individual conduct and by virtue of their positions as controlling persons of Wells Fargo under §20 of the Exchange Act.

109. During the Class Period, Defendants knowingly or recklessly engaged in a plan, scheme and course of conduct to cause and permit issuance of materially false and misleading statements and to conceal material facts in periodic reports, press releases and other publicly disseminated material.

110. During the Class Period, Defendants issued public statements and reports, including financial statements and other reports, releases and statements as described herein, which were materially false and misleading and in violation of those provisions of federal and state law. These reports, releases and statements were materially false and misleading in that they failed to disclose material adverse information about Wells Fargo's business, results from operations, operations earnings, financial condition, management and future business prospects.

111. Further, Defendants knew, or should have known but failed to disclose, that during the time of the Class Period, Wells Fargo would not be able to pay the projected earnings per share, but in fact would only be able to pay a minimal amount due to write-offs for bad investments and portfolio declines.

112. Additionally, by the commencement of and during the Class Period, Defendants knew, should have known or were reckless in and failed to disclose, that their prior favorable statements concerning Wells Fargo's position in the industry and expected financial performance were either untrue when made, were no longer true. Defendants also knew, or should have known and failed to disclose that these statements contributed to an overall misleading impression of the financial condition and business prospects of Wells Fargo. Nonetheless, despite the above, Defendants failed to make timely, corrective disclosures and failed to correct their misrepresentations concerning the earnings and profitability being experienced and expected to be experienced by Wells Fargo during 1991.

113. At all relevant times, Defendants had actual knowledge of the materially false and misleading statements and the material omissions set forth here, and intended to deceive Plaintiffs and other members of the Class, or in the alternative, acted with reckless disregard for the truth when they failed to disclose the true facts to Plaintiffs and other members of the Class.

114. Pursuant to §20(a) of the Exchange Act, the Individual Defendants were "control persons" with respect to Wells Fargo and were responsible for the disclosures made in the press releases, public reports and other publicly disseminated documents described more fully here. The Individual Defendants knew, or recklessly disregarded, the true financial and operating condition of the Wells Fargo's loan portfolio during the Class Period, which condition was concealed from Plaintiffs and the members of the Class throughout the Class Period.

115. As a result of the wrongful acts and material misstatements and omissions complained of here, the market price of Wells Fargo common stock was artificially inflated during the Class Period.

116. Following the belated and unexpected disclosure of Wells Fargo's true financial condition, the market price of Wells Fargo common stock declined sharply, causing substantial damages to Plaintiffs and the Class.

117. During the Class Period, Wells Fargo common stock was traded on an active and efficient market. Plaintiffs and members of the Class relied upon the truth and accuracy of the representation made by Defendants because of Defendants fiduciary responsibility and/or superior knowledge, and on the integrity of the market in purchasing Wells Fargo common stock during the Class Period. As a consequence of Defendants' wrongful conduct, Plaintiffs and the members of the Class were induced to, and in fact did, purchase their Wells Fargo stock at artificially inflated prices. Had Plaintiffs and members of the Class known the materially adverse information misstated or not disclosed by Defendants, they would not have purchased their stock at the artificially inflated prices they had paid or would not have purchased the shares at all.

118. By virtue of the foregoing, Plaintiffs and members of the Class have sustained substantial damages in an amount to be proved at trial.

SECOND CLAIM FOR RELIEF

(California Civil Code §1709 — Fraud and Deceit)

119. Plaintiffs reallege and incorporate paragraphs 1 through 117 above, as if set forth fully here.

120. Plaintiffs assert this Second Claim for Relief individually and on behalf of all members of the Class against all Defendants for fraud.

121. Each of the Defendants owed to purchasers of Wells Fargo common stock, including the Plaintiffs and the other members of the Class, a duty of full disclosure, honesty and complete candor, as well as a duty to exercise reasonable care and to make a reasonable and diligent investigation of the Annual Report and quarterly reports to shareholders and all reports regularly filed with the SEC.

122. For the purpose of inducing Plaintiffs and the members of the Class to purchase Wells Fargo common stock and with the intent to deceive such persons, Defendants employed a device, scheme and artifice to defraud. As part of said device, scheme and artifice to defraud, Defendants, and each of them, actively made and perpetrated, participated in the making or aided and abetted the making or perpetration of false and misleading statements and omissions of material fact as hereabove alleged. Each such statement and omission was untrue or misleading, and Defendants did not believe them to be true or not misleading when made or recklessly made such statements without regard to their truthfulness.

123. At the time said omissions and misrepresentations of material fact were made, Plaintiffs and the members of the Class were ignorant of the falsity of said statements and believed them to be true. In reliance upon said omissions and misrepresentations of material fact, and in ignorance of the true facts, Plaintiffs and the other members of the Class were induced to purchase, and, in fact, purchased Wells Fargo common stock. Had Plaintiffs and the other members of the Class known the true facts, they would not have purchased said securities.

124. As a direct and proximate result of the wrongful conduct alleged in this cause of action, Plaintiffs and the members of the Class suffered damages in an amount to be proved at trial.

125. Defendants' fraudulent conduct was wilful, malicious and oppressive, entitling Plaintiffs and the Class to punitive damages.

THIRD CLAIM FOR RELIEF

(California Civil Code §1710 — Negligent Misrepresentation)

126. Plaintiffs reallege and incorporate paragraphs 1 through 124 above, as if set forth fully here.

127. Plaintiffs assert this Third Claim for Relief individually and on behalf of all members of the Class against all Defendants for negligent misrepresentation.

128. Defendants owed to the purchasers of Wells Fargo common stock, including Plaintiffs and the other members of the Class, a duty of full disclosure, honesty, and complete candor, as well as a duty to exercise reasonable care and to make a reasonable and diligent investigation of the statements contained in the documents described above, including all public statements, filings and reports regarding Wells Fargo that were disseminated or filed during the Class Period. Defendants also owed Plaintiffs and other members of the Class a duty to correct any previously issued statements that became false as a result of subsequent events that took place during the Class Period.

129. In breach of these duties, Defendants and each of them, negligently and carelessly issued false statements concerning material facts, or omitted to state other material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, and failed to correct earlier statements that had become misleading.

130. Defendants disseminated to the Plaintiffs and members of the Class, uniform material misrepresentations regarding the financial condition of Wells Fargo.

131. Defendants made the false and misleading statements without a reasonable ground for believing them to be true and accurate.

132. The statements made by Defendants were issued for the purposes of inflating the market value of the Company's common stock.

133. Defendants' breach of their duty of care owed to Plaintiffs and the other members of the Class directly caused the price of Wells Fargo common stock to artificially inflate throughout the Class Period. Plaintiffs and the other members of the Class, who purchased Wells Fargo common stock during the Class Period, paid artificially inflated prices and suffered damages as a direct, proximate foreseeable result of Defendants' negligent misrepresentations.

134. As a proximate result of Defendants' negligent misrepresentations, Plaintiffs and members of the Class have been damaged in an amount to be proved at trial.

WHEREFORE, individual and representative Plaintiffs request of this Court the following relief, on behalf of themselves and all others similarly situated:

1. An order certifying the proposed Plaintiff Class here, under Federal Rules of Civil Procedure 23(a) and 23(b)(3), and appointing Plaintiffs and their counsel of record to represent the Class;

2. An award of money damages against Defendants jointly and severally, in favor of Plaintiffs and the other members of the Class for all losses and injuries suffered as a result of the acts and transactions complained of here, together with pre-judgment interest on all such damages which the Court shall award from the date of the wrongs to the date of judgment at the maximum rate permitted by law;

3. An award of punitive damages;

4. An award of costs and disbursements of this action, including reasonable allowances of fees for Plaintiffs' attorneys and experts and reimbursement of Plaintiffs' expenses; and

5. Granting Plaintiffs equitable relief including an attachment and/or a freeze of the Defendants' assets and/or injunctive relief against the disposition of these assets; and

6. Such other and further relief as the Court may deem just and proper.

DATE: August 26, 1991

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[Demand for Jury Trial omitted]

RULES INVOLVED

Rule 9(b), Federal Rules of Civil Procedure:

> **(b) Fraud, Mistake, Condition of the Mind.** In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other conditions of mind of a person may be averred generally.

Rule 12(b), Federal Rules of Civil Procedure:

> **(b) How Presented.** Every defense, in law or fact, to a claim for relief in any pleading, whether a claim, counterclaim, cross-claim, or third-party claim, shall be asserted in the responsive pleading thereto if one is required, except that the following defenses may at the option of the pleader be made by motion: (1) lack of jurisdiction over the subject matter, (2) lack of jurisdiction over the person, (3) improper venue, (4) insufficiency of process, (5) insufficiency of service of process, (6) failure to state a claim upon which relief can be granted, (7) failure to join a party under Rule 19. A motion making any of these defenses shall be made before pleading if a further pleading is permitted. No defense or objection is waived by being joined with one or more other defenses or objections in a responsive pleading or motion. If a pleading sets forth a claim for relief to which the adverse party is not required to serve a responsive pleading, the adverse party may assert at the trial any defense in law or fact to that claim for relief. If, on a motion asserting the defense numbered (6) to dismiss for failure of the pleading to state a claim upon which relief can be granted, matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56, and all parties shall be given reasonable opportunity to present all material made pertinent to such a motion by Rule 56.